This is a digital copy of a book that was preserved for generations on library shelves before it was carefully scanned by Google as part of a project to make the world's books discoverable online.

It has survived long enough for the copyright to expire and the book to enter the public domain. A public domain book is one that was never subject to copyright or whose legal copyright term has expired. Whether a book is in the public domain may vary country to country. Public domain books are our gateways to the past, representing a wealth of history, culture and knowledge that's often difficult to discover.

Marks, notations and other marginalia present in the original volume will appear in this file - a reminder of this book's long journey from the publisher to a library and finally to you.

Usage guidelines

Google is proud to partner with libraries to digitize public domain materials and make them widely accessible. Public domain books belong to the public and we are merely their custodians. Nevertheless, this work is expensive, so in order to keep providing this resource, we have taken steps to prevent abuse by commercial parties, including placing technical restrictions on automated querying.

We also ask that you:

+ *Make non-commercial use of the files* We designed Google Book Search for use by individuals, and we request that you use these files for personal, non-commercial purposes.

+ *Refrain from automated querying* Do not send automated queries of any sort to Google's system: If you are conducting research on machine translation, optical character recognition or other areas where access to a large amount of text is helpful, please contact us. We encourage the use of public domain materials for these purposes and may be able to help.

+ *Maintain attribution* The Google "watermark" you see on each file is essential for informing people about this project and helping them find additional materials through Google Book Search. Please do not remove it.

+ *Keep it legal* Whatever your use, remember that you are responsible for ensuring that what you are doing is legal. Do not assume that just because we believe a book is in the public domain for users in the United States, that the work is also in the public domain for users in other countries. Whether a book is still in copyright varies from country to country, and we can't offer guidance on whether any specific use of any specific book is allowed. Please do not assume that a book's appearance in Google Book Search means it can be used in any manner anywhere in the world. Copyright infringement liability can be quite severe.

About Google Book Search

Google's mission is to organize the world's information and to make it universally accessible and useful. Google Book Search helps readers discover the world's books while helping authors and publishers reach new audiences. You can search through the full text of this book on the web at `http://books.google.com/`

Y 4.B22/1:100-70

MONEY LAUNDERING CONTROL ACT AMENDMENTS OF 1988

ON-RECORD ONLY

HEARING

P108-92

BEFORE THE

COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS HOUSE OF REPRESENTATIVES

ONE-HUNDREDTH CONGRESS

SECOND SESSION

JUNE 8, 1988

Printed for the use of the Committee on Banking, Finance and Urban Affairs

Serial No. 100-70

STANFORD LIBRARIES

STANFORD UNIVERSITY JAN 1989 JOHNSON LIBRARY OF GOVT DOCUMENTS

U.S. GOVERNMENT PRINTING OFFICE

Digitized by Google

HOUSE COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS

FERNAND J. ST GERMAIN, Rhode Island, *Chairman*

HENRY B. GONZALEZ, Texas
FRANK ANNUNZIO, Illinois
WALTER E. FAUNTROY, District of Columbia
STEPHEN L. NEAL, North Carolina
CARROLL HUBBARD, JR., Kentucky
JOHN J. LAFALCE, New York
MARY ROSE OAKAR, Ohio
BRUCE F. VENTO, Minnesota
DOUG BARNARD, JR., Georgia
ROBERT GARCIA, New York
CHARLES E. SCHUMER, New York
BARNEY FRANK, Massachusetts
RICHARD H. LEHMAN, California
BRUCE A. MORRISON, Connecticut
MARCY KAPTUR, Ohio
BEN ERDREICH, Alabama
THOMAS R. CARPER, Delaware
ESTEBAN EDWARD TORRES, California
GERALD D. KLECZKA, Wisconsin
BILL NELSON, Florida
PAUL E. KANJORSKI, Pennsylvania
THOMAS J. MANTON, New York
ELIZABETH J. PATTERSON, South Carolina
THOMAS McMILLEN, Maryland
JOSEPH P. KENNEDY II, Massachusetts
FLOYD H. FLAKE, New York
KWEISI MFUME, Maryland
DAVID E. PRICE, North Carolina
NANCY PELOSI, California
GARY L. ACKERMAN, New York

CHALMERS P. WYLIE, Ohio
JIM LEACH, Iowa
NORMAN D. SHUMWAY, California
STAN PARRIS, Virginia
BILL McCOLLUM, Florida
GEORGE C. WORTLEY, New York
MARGE ROUKEMA, New Jersey
DOUG BEREUTER, Nebraska
DAVID DREIER, California
JOHN HILER, Indiana
THOMAS J. RIDGE, Pennsylvania
STEVE BARTLETT, Texas
TOBY ROTH, Wisconsin
AL McCANDLESS, California
J. ALEX McMILLAN, North Carolina
JAMES SAXTON, New Jersey
PATRICK L. SWINDALL, Georgia
PATRICIA SAIKI, Hawaii
JAMES BUNNING, Kentucky
JOSEPH J. DIOGUARDI, New York

Digitized by Google

CONTENTS

Digitized by Google

Digitized by Google

MONEY LAUNDERING CONTROL ACT AMENDMENTS OF 1988

Wednesday, June 8, 1988

HOUSE OF REPRESENTATIVES,
COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS,
Washington, DC.

The committee met at 2:10 p.m. in room 2128 of the Rayburn House Office Building, Hon. Fernand J. St Germain [chairman of the committee] presiding.

Present: Chairman St Germain, Representatives Torres, Hubbard, Parris, Wortley, McMillan, Pelosi, Wylie, Price, Carper, Barnard, Bartlett and Garcia.

The CHAIRMAN. The committee will come to order.

This afternoon, this committee reopens its efforts to protect against U.S. banks being used, wittingly or unwittingly, to launder the profit from international drug trafficking.

It is news to know, one, that drugs generate massive sums of cash. This cash must be laundered, slipped into the mainstream of commerce—if the drug traffickers are to be successful.

We intend to make these laundering operations as difficult and costly as possible. We cannot allow financial institutions, insured by the U.S. Government, to be used whether by accident or design.

Long before the war against drugs became so popular—when it was still a skirmish—this committee initiated the Bank Secrecy Act to require the reporting of large cash transactions. We launched that legislation in 1969—almost 2 decades ago—and it has proved valuable in tracking funds originating from drug operations.

Through the years, including the Anti-Drug Abuse Act of 1986, we have beefed up this law and we have pushed consistently in oversight hearings to upgrade enforcement of the reporting requirements.

But, much more needs to be done.

We have before us a Committee Print that would require appropriate identification for individuals purchasing money orders, cashiers' checks and related instruments of $3,000 or more.

In too many cases drug operators are moving undetected from bank to bank with purchases of monetary instruments that fall below the threshold of current reporting requirements. Our Colleague from California, Mr. Torres, deserves great credit for pushing this $3,000 provision.

The legislation would also authorize the Secretary of the Treasury to target an individual institution or institutions in a geo-

Digitized by Google

graphical area for additional recordkeeping where the drug activity is heavy and large cash sums are being generated.

A third provision would allow law enforcement agencies to inspect the records of bank insiders suspected of being involved in criminal activity against the bank—without the insiders being tipped under the provisions of the Right to Financial Privacy Act.

Thus, if an insider was involved in a conspiracy to hide cash transactions and facilitate the laundering of money, law enforcement agencies could move quickly before records were destroyed or altered by insiders and their confederates warned.

This legislation will send a further strong—and I hope unmistakable—signal that financial institutions are off-limits for the drug merchants.

This afternoon we will have testimony from Gerald L. Hilsher, Deputy Assistant Secretary, Law Enforcement, accompanied by Amy G. Rudnick, Director, Office of Financial Enforcement, Department of Treasury; and Victoria Toensing, Deputy Assistant Attorney General, Criminal Division, accompanied by Charles Saphos, Chief, Narcotic and Dangerous Drug Section, Criminal Division, Department of Justice.

The CHAIRMAN. Mr. Torres, did you have a statement?

Mr. TORRES. Thank you, Mr. Chairman. I would like to thank you for holding this hearing today, and for the expeditious consideration of this legislation, which the full committee will mark up tomorrow.

I have been pleased in particular at the dialogue and the cooperation we have had with the Department of the Treasury in working to develop these amendments, to shut down the operations of smurfers, those who are using our Nation's banks to conceal illegal drug profits.

The law enforcement community has indicated their support for this committee's efforts to help investigate, apprehend and prosecute money launderers.

Today, I met with members of the staff of the FBI and the DEA, again voicing concerns about these problems.

The 1986 Omnibus Drug Act included a number of provisions that make it much more difficult for money launderers to carry out their schemes in our Nation's banks.

However, cash transactions involving drug money, primarily in amounts of between $3,000 and $10,000, are still prevalent. And so we need additional deterrents.

The Committee Print contains provisions which are workable and useful deterrents. Requiring identification to be shown by nonaccount holders when purchasing in particular monetary instruments most often used by money launderers, would be a deterrent to the smurf. And we all know what those instruments are:

Cashiers checks, bank checks, travelers checks and, money orders. Now, requiring identification is not seen as an obstacle to those individuals who are conducting legitimate transactions.

The targeting provision allows the Treasury Department to call for additional recordkeeping at specific banks or those in a particular geographic area, where there appears to be a high degree of drug money laundering activity.

Digitized by Google

This provision is intended to be of a limited time duration, enough to clear launderers out of a specific area.

I know that, while we cannot stop every instance of money laundering, it is clear that more can be done to stop the use of financial institutions by the drug elements in our society and we aim to do that in this particular legislation.

So, Mr. Chairman, I look forward to hearing the testimony of our witnesses today.

Thank you.

The CHAIRMAN. Our first witness will be Secretary Hilsher. We will put your entire statement in the record and you may proceed.

STATEMENT OF GERALD L. HILSHER, DEPUTY ASSISTANT SECRETARY, LAW ENFORCEMENT, DEPARTMENT OF THE TREASURY; ACCOMPANIED BY AMY G. RUDNICK, DIRECTOR, OFFICE OF FINANCIAL ENFORCEMENT, DEPARTMENT OF THE TREASURY

Mr. HILSHER. Thank you. I would also like to introduce Amy Rudnick to my right. She is the Director of the Treasurer's Office of Financial Enforcement, and has been in that position since November of 1987.

Thank you for including my prepared remarks in the record. At this point, I would like to summarize a few key points.

I am pleased to have the opportunity to testify before the committee today about the committee's draft bill which would revise the Secrecy Act and the Right to Privacy Act. We understand this bill will be put forward by the committee for inclusion in the House Omnibus Drug Legislation.

As you know, the President has recommended the creation of a special bipartisan Executive/Legislative Task Force to advance a unified response to the drug problem.

The administration firmly believes that, in order to effectively combat all aspects of illegal drug-trafficking and use, the legislative and executive branch must work together to review every area of the drug problem and to develop a coordinated legislative strategy.

Thus, while the Department of the Treasury is generally in agreement with the committee's bill, we strongly urge you to remain flexible in considering any and all legislation that is aimed at fighting one front, albeit an important front, of the war against drugs.

Before we begin, I want to commend you, Mr. Chairman, and the committee for your continued interest in effective administration and enforcement of the Bank Secrecy Act.

Over the years, you and the committee have played a vital role in making the financial community aware of its responsibilities for full compliance with the Bank Secrecy Act and of the consequences of violating its requirements.

You also have been responsive when Treasury has sought to enact new legislation to enhance its authority for ensuring compliance with the act, and to prevent money-laundering activities.

The committee's bill sets forth two new Bank Secrecy Act provisions, 31 U.S.C. 5324 and 5326. First, I would like to discuss proposed section 5325, which is aimed at one method of money laun-

Digitized by Google

dering, specifically "smurfing," through the cash purchase of monetary instruments—cashiers' checks, bank checks, travelers' checks and money orders. This provision was drafted by Congressman Torres.

The intent of proposed section 5325 is to require identification from money launderers who are not account holders at the financial institutions where they purchase monetary instruments with cash.

Under the Bank Secrecy Act, the only identification records currently required for individuals who do not engage in currency transactions in excess of $10,000 are those that pertain to new accounts. Thus, under the Act, a customer who does not have an account relationship with a financial institution can engage in currency transactions under the $10,000 reporting threshold without being detected by the Government and, often, by the financial institution itself.

Proposed section 5325 would require financial institutions to obtain identification and maintain a record of cash purchases of these monetary instruments by nonaccount holders. To comply with this requirement, Treasury envisions that financial institutions would need merely to maintain a chronological log of the cash purchases of these instruments. This log would be reported to Treasury upon request.

Treasury believes that the requirements of proposed section 5325 will be a useful deterrent to the practice of smurfing through the purchase of monetary instruments and will not be overly burdensome for financial institutions.

In fact, Treasury has recommended that a proposal similar to Congressman Torres' proposal be included in the administration's recommended legislative proposals being developed in the National Drug Policy Board.

Treasury does, however, have some recommendations that we believe would improve section 5325. First, we recommend that Treasury's authority to require the financial institution to provide Treasury with a report of the identification information it has obtained be made explicit in the statute.

Second, we urge the committee to delete any reference to a specific dollar amount at which the identification information would be required from the statute.

Rather, we would prefer for the Secretary of the Treasury to be given the authority to determine an appropriate amount by regulation. In this way, Treasury will be able to respond more easily to changing law enforcement needs.

Under the second proposed provision, section 5326, the Secretary of the Treasury would be able to issue an order to target financial institutions in certain geographic locations for special reporting of currency or monetary instrument transactions in an amount less than $10,000 for a limited period of time.

The location would be selected based upon a determination by the Secretary that there may exist a high level of drug money laundering activity in that area.

A request from a Treasury law enforcement "currency group" or joint financial investigative task force would trigger such a determination.

Digitized by Google

Under this proposal, Treasury would be able to require all financial institutions to file currency reports at an amount lower than the normal $10,000 reporting threshold under the Bank Secrecy Act. The purchasers of these instruments would have to provide the identification, and other pertinent information required under the Bank Secrecy Act.

Treasury envisions that the form to be used for making these reports would be the Currency Transaction Report, CTR, which is filed on form 4789, and that no new form would be developed. The report then would be separated from the usual CTRs and analyzed by a team of Treasury investigators or analysts working in the currency group or in a joint financial task force in the targeted location.

Because time would be of the essence in maximizing the utility of the information obtained pursuant to a targeting order, Treasury is pleased to see that the bill exempts any order issued pursuant to proposed section 5326 from the normal delayed effective date provisions required for regulations under the Administrative Procedure Act (APA).

The implementation of a request to target a limited geographic area does present some practical problems for Treasury as well as the affected financial institutions.

First, Treasury would have the responsibility for quickly identifying all the financial institutions to be targeted in the specific geographical area.

While it would not be difficult for Treasury to identify the affected banks, it would be difficult for Treasury to identify certain categories of nonbank financial institutions, that is, currency exchanges and check cashers.

Second, Treasury would have to transmit notice of the order by letter to all the affected institutions.

Finally, the targeted institutions would have to educate their tellers and other employees very quickly, as to the new reporting requirements and any additional recordkeeping requirements.

Despite the practical difficulties in implementing any order, Treasury believes that the information obtained could be highly useful to law enforcement officials.

On-the-spot analysis of the information may very well lead to the breakup of money laundering organizations.

For this reason, Treasury is anxious to develop and refine the concept. Treasury recognizes, however, that a significant drawback to any approach that is limited geographically will result in driving money launderers on to new locations where law enforcement officials and financial institutions may not be as sensitive to patterns of money laundering.

While we cannot judge with certainty the outcome of this kind of targeting, Treasury hopes that next year, we will be able to come back and report favorably to the committee on its utility.

In addition to the amendments to the Bank Secrecy Act contained in the committee's bill, Treasury hopes that you will consider including a number of technical corrections to the Money Laundering Control Act of 1986, Subtitle H of the Anti-Drug Abuse Act of 1986, Pub. L. 99-570, in the bill.

Digitized by Google

My staff has provided draft language to the committee staff and discussions are ongoing on these technical revisions.

I would like to turn now to the committee's proposed amendments to the Right of Financial Privacy Act.

While Treasury shares the committee's concern with protecting the financial privacy of individuals, Treasury believes that, in today's climate, we must in some limited areas reevaluate the appropriate balance between the right to financial privacy and the legitimate needs of Federal law enforcement. Treasury remains sensitive to protecting the privacy rights of individuals within the context of law enforcement needs.

Treasury is very pleased that the bill includes a revision to the RFPA that would allow information and records relating to possible crimes against financial institutions or supervisory agencies by insiders to be provided by the financial institutions or supervisory agency to the Justice Department without notice to the insider.

We fervently agree with you on the need for this measure. The draft bill similarly provides a possible violation by insiders of the Bank Secrecy Act, that they may be reported to the Secretary of the Treasury without notice, at least with respect to officers, directors and employees.

Existing law already clearly authorizes such disclosures. We strongly urge you to emphasize in the Committee Report that this is not a change in existing law. An amendment to the RFPA is very much needed to provide financial institutions to not only report possible violations of the Bank Secrecy Act by their customers, that is, in situations where the bank suspects that its customers have violated the Bank Secrecy Act's anti-structuring provisions, but also to provide bank records and other information.

If the bank is not implicated in the anti-structuring violation, broad disclosure to Treasury may not be within the exercise of Treasury supervisory functions.

Banks then only would be able to provide Treasury with the limited suspicious transaction information allowed by Section 1103(C) of the RFPA, and generally, without access to the underlying customer account records and other information, this information may not be adequate to establish probable cause that the anti-structuring provisions have been violated.

Without such probable cause, Treasury must issue a summons to the institution for the information and provide notice to the customer. Notice to the customer would be fatal because once the customer has knowledge of the summons, he can withdraw the money on deposit or wire-transfer it to a foreign jurisdiction.

For these reasons, we urge you to include a provision in the RFPA that would allow a financial institution to report in good faith all available information and to disclose records with respect to possible violations of the Bank Secrecy Act by customers without notice to the customer and without fear of civil liability.

Cooperation from the financial community is an increasingly important aspect in the attack against the financial infrastructure that supports the drug trade.

Just recently, 45 tons of marijuana and hashish were seized in San Francisco on the barge Intrepid Voyager. This seizure was a direct result of referrals by the North Napa Branch of the Bank of

Digitized by Google

America and other banks to the IRS of suspicious transactions by a customer who appeared to be circumventing the CTR reporting requirements.

In addition to the drug seizure, at least six individuals have been arrested and over $1 million in cash, three vessels and real property have been seized.

I would like to take this opportunity to extend the Treasury Department's appreciation to the Bank of America and all other financial institutions that are providing reports of suspicious financial activity to IRS and Customs, to further encourage the reporting of such suspicious transactions.

Within the next 2 weeks, IRS will be introducing a suspicious transaction number: 1-800-BSA-CTRS; a similar toll free number for Customs, 1-800-BE ALERT, has been operational for sometime.

In conclusion, Mr. Chairman, we are fighting a war with many fronts in the war against drugs. But our goals are clear. We share the goal of this committee to close the doors of legitimate financial institutions to launderers. We believe the most effective way to do this is as a part of a coordinated executive/legislative drug strategy.

For this reason, we strongly encourage you to work with the Executive/Legislative Drug Task Force to achieve a unified response to all aspects of the drug problem.

We also want financial institutions to be partners with Treasury in achieving this goal. In turn, we will act responsibly in balancing law enforcement needs with the cost of financial institutions in exercising our regulatory authority.

We also seek to maximize efficiency and effectiveness in the use of the Bank Secrecy Act.

Mr. Chairman, I would be pleased to answer any questions that any Member of the committee might have. Thank you for your attention.

[The prepared statement of Gerald Hilsher can be found in the appendix.]

The CHAIRMAN. Thank you, Mr. Secretary. We are being summoned to the floor for a vote, so we will go to vote and then return. And at that time take testimony from Justice.

We will be in recess for 5 minutes or so.

[Recess.]

The CHAIRMAN. Our next witness will be Ms. Victoria Toensing, Deputy Assistant Attorney General, Department of Justice, accompanied by Charles Saphos, Chief of the Narcotic and Dangerous Drug Section, Criminal Division of the Department of Justice.

We will put your entire statement in the record and you may proceed.

STATEMENT OF VICTORIA TOENSING, DEPUTY ASSISTANT ATTORNEY GENERAL, CRIMINAL DIVISION, DEPARTMENT OF JUSTICE; ACCOMPANIED BY CHARLES SAPHOS, CHIEF, NARCOTIC AND DANGEROUS DRUG SECTION, CRIMINAL DIVISION, DEPARTMENT OF JUSTICE

Ms. TOENSING. It is only appropriate that the person I brought from the Justice Department, Mr. Saphos, is the father of the

Digitized by Google

person who named smurfing. It was done, and I will let him explain it later, but done as only—it could be, on a Saturday when a parent is working and brings the child with him. And he is watching television and the smurfs are on and he is arresting money launderers.

I will let him finish it.

I am very delighted to share with you the Department of Justice's views on your committee's initiatives to protect financial institutions from being used by dope dealers.

I thank you for asking me. I also want to add another thanks, and that is for the 1986 legislation, which has been a useful tool for us in combating this area in money laundering.

Very specifically, we appreciate the money laundering offenses in 18 U.S.C. 1956 and 1957, and the Right to Financial Privacy Act and Currency Reporting Act amendments. To us, one of the most important 1986 changes in the Right to Financial Privacy Act is that now financial institutions can give to law enforcement at least limited information about possible criminal violations.

Before those amendments, we could get nothing, no information. So we in law enforcement had the ludicrous situation where a financial institution suspected a crime but could not tell law enforcement about it.

So, thank you. But we need some more fine-tuning, Mr. Chairman. So we have come back to the well, so to speak, wanting a few more changes to the RFPA.

There are three main areas that I would like to address. I will just outline them very briefly and then discuss them just a little bit more in depth.

The first one is when financial institutions have records. We want access to those records of insiders and major borrowers. And we don't want notice to go to these people.

The second is when agencies have possession of the records. And we are also concerned that in that situation we could have notice going to those people who are being investigated when those records come over to law enforcement.

The third area is where we have voluminous grand jury records and we have to actually physically present them before the grand jury, we would like some relief in that area.

So let me just discuss each one of those a little bit more in depth.

When a financial institution has the records in its possession, we cannot get those records of wrong-doing without either a grand jury subpoena or some other kind of legal process. We cannot get the records of anyone if we suspect them of being involved in criminal activity.

If we acquire the records by this other legal process, then notice goes to the suspects informing them that we are investigating them.

In sum, we either have to launch a grand jury investigation and use up grand jury time or we have to give notice to the suspect. That is what we are faced with. And w eel that that is a Hobson's Choice for us in this kind of in ion.

We feel that the integrity tutions is important that we need to obtain evi cklv id as efficiently as possible. So, t like to in-

Digitized by Google

clude major borrowers in the definition of "insiders", Mr. Chairman, in other words, those who become so inextricably intertwined in the dealings and the solvency of the financial institution.

If they are conducting criminal activity and ripping off the financial institutions, we feel that they should not be given the protection of the RFPA.

The second area is somewhat related. It has to do with notice, but from another aspect. And that is when agencies have possession of these records of a crime or criminal activity by one of the institution's customers.

Right now, the law requires that if an agency sees evidence of a crime, they cannot turn the records over to the Department of Justice without giving notice to the suspects.

Let me explain a situation where that could very easily occur.

For example, a bank regulatory agency takes over a failed institution and finds evidence of fraud. Right now, they have to give notice to those persons whose records are being turned over to law enforcement.

We appreciate with you the concern about the right to privacy and the protection that this act affords.

However, in this kind of a situation, the Government agency already has the records, so we're really not providing any more protection. The Government already has the records and can see the fraud.

The only thing that is being inhibited under this rule is that law enforcement cannot know about the crime, and so we ask relief from that kind of restriction.

The third area is the problem of the voluminous grand jury records. The way that the RFPA, the Right to Financial Privacy Act, is written—and no other law requires this, we have no other requirement for the grand jury—is that the prosecutor or the agent has to bring, physically, actually bring in hundreds of thousands of documents at times, and actually physically present them before the grand jury.

Sometimes, that is impossible and so we have to bus the grand jury to the place where all of the records are being kept.

In these days of Gramm-Rudman where many districts now only have grand juries meeting once a month, 1 day a month, this is a terrible waste of their time to have to do this, to have to go through this kind of a ritual. And we would like some relief from that requirement.

What we have done is attach three draft amendments for the committee. We think these amendments would cure the three problems that I have just addressed.

We also have two rather technical but important problems for us under 18 USC section 1956 and 1957, and I will just address those very briefly.

The first one is that, under section 1956, we have a problem in that we cannot run a sting operation because section 1956 requires that in order for there to be an offense that the financial transaction, in fact, has to involve the proceeds of unlawful activity. And we cannot use a sting activity because of course that would be the Government running it and it would not be, in fact, unlawful activity.

Digitized by Google

So we need that changed. And we would help work with the committee on that.

The second, in section 1956 and 1957 there is a requirement that money has to be in bearer form. So, if a dope dealer buys a boat with cash, he can be caught under the act. But, if he puts it through the bank, writes a check for the boat with the money, then he is not subject to the act.

We would like those two rather technical, but as you can see, very important amendments addressed.

I would like to close by saying, Mr. Chairman, that I was a federal drug prosecutor in Michigan in the 1970's, back at the time when it was not very fashionable to go after dope dealers, and where I was chastised by various people for taking a cocaine case because, after all, it was just a recreational drug. And so I have seen for a good many years the problems that we encounter in this drug area.

I share with the committee the concern for these issues being addressed in a systemized fashion.

With that concern, I also support Mr. Hilsher's request that the committee address the bipartisan Executive/Legislative Committee that the President has requested to work on this issue because only in doing it, where one thing flows from another, will we be able to really address this terrible problem of drugs.

I would be delighted to answer any questions the committee might have.

[The prepared statement of Victoria Toensing can be found in the appendix.]

The CHAIRMAN. We have to have Mr. Saphos explain the origin of smurfing. I have been waiting with baited breath.

Mr. SAPHOS. Three of the people in the audience from the banking community have said:

If I hear one more time the origin of the word "smurf", I'm walking out.

That is one of the things I precede my talks to the banking community with, and I also introduce myself as the SOB who is involved in indicting bankers for violating the law.

When we first noticed this phenomenon, I was a narcotics prosecutor in south Florida. I was in charge of a thing called Operation Greenback. The phenomenon was that groups of persons would start up the road in north Florida and work down the road by hitting all of the banks. At each of the banks, they would make a cash transaction of less than $10,000, right under the reporting limit.

It appeared that afterwards—thanks to the work of this committee and thanks to the work of the investigators and prosecutors—the doors of the banks were closed in south Florida to the massive amount of depositors who were bringing in suitcases and bags full of money. The number of money launderers had multiplied geometrically down there and they were all busily running from bank to bank. And their activities were so pervasive that it was very much like the numerous and fast-acting little cartoon characters that my son was watching on TV one Saturday morning in the office, when we were tryi to launch teams to this p omenon.

It was his r ere doing, that these cl

Digitized by Google

It is probably a violation of several copyrights and certainly probably demeans some attractive cartoon characters, but it has caught on.

The CHAIRMAN. Well, I will tell you I have never heard of a cartoon character named Smurf, so it doesn't really matter.

We have heard a lot about smurfing and smurfers in this committee, testimony that we have taken on the legislation that we enacted the last time, and previously.

I would say to both witnesses and their accompanying individuals: the American Banker in a June 7 article, as well as a letter to committee Members, alludes to the fact that money-laundering structuring transactions are not a bank problem, quote:

"The structure is designed to work against—isn't going on in banks any more. Everything that we are hearing is that this is going on in casinos and other places at this point in time."

First, Ms. Toensing, I would ask Justice is this a fact? The smurfers, the drug traffickers? Have they ceased using financial institutions and have they just gone to casinos to convert their cash into checks and then transport it back to their countries of origin?

Ms. TOENSING. We have made it much harder for them to go to banks, so they are looking for other arenas; not only to gambling casinos, I think they will probably go a lot to Indian reservations and gambling casinos because Congress hasn't yet made requirements for that area—I just thought I would get a plug in for another area I have to testify a lot about.

But we contend that wherever you start loosening the rules, or you don't tighten them, you will have problems. It is only an argument for tightening up the situation elsewhere as well as for banks.

Maybe Mr. Saphos would like to add something to that.

Mr. SAPHOS. Indeed, it could well be true that money launderers are attracted to casinos. But the fact of life is there are one heck of a lot more banks than casinos and money launderers are still going to be doing transactions of less than $10,000 in the institutions.

The CHAIRMAN. Mr. Hilsher.

Mr. HILSHER. Mr. Chairman, I think it is a gross overstatement to say that, as a result of the structuring statute that the smurfs have left the banks. Quite to the contrary, we continue to receive reports of suspicious activity from the banks, some 300 reported to OCC and FDIC, the majority of which were suspicious transactions related to structuring to evading the reporting requirement.

So it is still out there and it is still in the banks. Fortunately, we have sensitized the banks through strong enforcement actions and by this committee's oversight. We have sensitized the banks to the problem and they are reporting suspicious transactions to us.

But it has not left the banks and we do need to be cautious that it doesn't go to other locations like casinos, currency exchanges and check cashers.

The CHAIRMAN. Now, in line with that, as we know, there has been a large increase in the reports being filed, the CTRs, since the hearings we had on the Bank of Boston. And I'm told that the banks are filing about 600,000 CTRs a month.

Digitized by Google

Has the Detroit processing center been able to catch up with this added volume? And are the financial institutions unduly burdening the reporting system?

In other words, are they prudently reporting CTR data?

Mr. HILSHER. Mr. Chairman, the Detroit data center has been able to keep up with this large number of CTRs that are coming into the system. However, we are concerned that there are a large number of reports coming in to Detroit that need not come into Detroit, that could be exemptible by the banks.

Unfortunately, the banks are cautious. They don't want to be subjected to the stringent civil penalties of the Treasury Department and they may be over-filing as a result of that.

Our office has determined that, to better educate the banks on the process of exempting those customers who, under the regulation, should be exempted, we have currently at the printers at the Government Printing Office an exemption handbook which will be available for the financial institutions for purchase at some nominal charge, hopefully to better attune them to that situation.

So we think we are handling the problem currently, but if we can continue to see this massive over-reporting, we are going to have to ask for more people, more machinery, and so forth, to handle it. We want the information that we have determined is useful, not just a bunch of data that just clogs up the processing system.

I think—I gave a talk to the American Bankers Association in Atlanta a couple of weeks ago. They were all very interested in receiving this exemption handbook. I think it will go a long way, sir.

The CHAIRMAN. Ms. Toensing, when you use the term "major borrower" in one of the amendments that you have appended to your testimony that you would like us to consider, describe to us what you feel is a major borrower.

I am concerned that we may have a little problem with that definition.

Ms. TOENSING. I appreciate that, Mr. Chairman. We are flexible. We can sit down and talk with the committee. The term, I think what we propose was a loan for $500,000, as someone being on the threshold of a major borrower. But we will listen to other sums, too. I think the chairman wants it a bit higher than that.

But it is our feeling that major borrowers many times are like nsiders. They are so involved in the inner workings of the bank. If hey are not looked at like an insider when reneging on their loans or money laundering, they can affect the workings of the financial institution in the same way that an insider can.

Many times, major borrowers are so closely aligned with insiders that, when notice is given to a bank that records are being turned over, it is like giving notice again to the person who is being investigated. Although the person may not have the title of being an insider, the fact that he is such a major borrower could mean that he is really involved in the workings of the financial institution.

The CHAIRMAN. Mr. Wylie?

Mr. WYLIE. Thank you, Mr. Chairman.

That was a good question. That is one I was going to ask. But I will go to my second one.

Digitized by Google

The financial institutions are saying that they are already required to report known or suspected crimes against the institution on the criminal referral forms. These are very detailed reports and cover insiders, and they want to know why you are asking the financial industry to hand over actual records.

Are the criminal referral forms not enough? Aren't they effective, Ms. Toensing?

Ms. TOENSING. I am glad you asked that question. That is a good one also, one that we should get involved in.

I have read their statement where they say they give extensive information. I guess it is all in the eyes of the beholder. But we wouldn't view it as extensive information. It is very limited information. It is just enough to permit us in law enforcement to say, "Well, now we can ask for a grand jury subpoena in this area and find out what is really there."

We believe that we should not have to go into the grand jury, launch a grand jury investigation, in order to make what we consider is a preliminary decision as to whether an investigation should proceed.

Maybe Mr. Saphos would like to add something to that, because as head of narcotics he does those kinds of cases.

Mr. WYLIE. Mr. Saphos?

Mr. SAPHOS. Thank you, sir.

Two things come to mind. First of all is the cost of initiating a grand jury investigation based upon the belief of a non-law enforcement person that there may be criminal activity afoot. We wish to encourage those banking officers and employees who believe criminal activity may be afoot to confer with us on that matter. But they are restricted to the extent they can confer with us by the law as it is now.

What we would like to do is to be able to loosen that up so that they can show us documents that support their contentions so that we can make the preliminary determination of whether an expensive grand jury investigation is appropriate.

Second, with a class of persons, those whose activities are inextricably intertwined with that of the bank, giving notice to the bank of the existence of an investigation—that is, a grand jury subpoena or an administrative subpoena with notice requirements—gives notice to those individuals that the game is up. And in many institutions we see where their accounts have been emptied and where they have departed to places south as a consequence of having done that.

I had a file cabinet of those cases that we used to call the "also-run," because each of the defendants like the ones before ran back to Colombia with their wealth when they found out we were investigating them.

Mr. WYLIE. Mr. Hilsher, it is my information that we are not getting very much cooperation in the international market as far as money laundering is concerned.

It is also my understanding that the administration has been working hard to include all aspects of the narcotics problem in the upcoming economic summit in Toronto.

Are you in on any of those recommendations, or have you made any, or will the United States be making some recommendations at

Digitized by Google

that summit? It seems like to me that is a good place to bring it into the forefront.

Mr. HILSHER. I agree with you, Congressman. It is the perfect opportunity to get our summit seven partners with us, and in broadcasting the importance of the drug problem and the money laundering part of that, I participated as the moderator at the international money laundering panel that was held during the White House Conference for a Drug-Free America. Many of the concepts that were brought forward in that international arena have been briefed for the Secretary and for the sherpas that are leading this effort, trying to get it on the agenda.

The narcotics—our administration has raised the narcotics issue, and the narcotics will be discussed in Toronto because of the recognized urgent need for international cooperation on a variety of programs to counter all aspects of the problem.

What we are recommending is that there be created an experts panel to be conducted after the formal meeting of the summit to work on these and other initiatives that came out of the White House Conference for a Drug-Free America, to give added emphasis to the U.N. Conventions, the Organization of American States, the European Community, and a variety of international organizations that are working on money laundering and drug trafficking issues right now.

Mr. WYLIE. Thank you. That sounds very encouraging.

Thank you, Mr. Chairman.

The CHAIRMAN. Mr. Torres?

Mr. TORRES. Thank you, Mr. Chairman.

I would like again at this time to commend the Treasury Department, Mr. Hilsher and Ms. Rudnick for their good work in working with my staff and me in developing an understanding of what is needed here.

I would like to ask, Mr. Hilsher, in regard to compliance with section 2 of the Committee Print, your testimony on page 3 indicates that banks would maintain a simple chronological log of the cash purchases of these particular instruments that we are talking about.

Could you tell me what kind of log that will be? Will that be some form of a note that the teller makes? Is it a computer entry? Is there going to be some form involved, a printed form? What will it be?

Mr. HILSHER. Congressman, we do not anticipate the creation of a new form in any way similar to an IRS form 4789 or anything such as that.

But commonly in many banks, when one goes in to purchase a monetary instrument, especially when you are an account holder, there is a record that is created at the time of the purchase. And the check, the actual check, is peeled off of that carbon, three-part carbon copy.

We are talking about that type of form that would indicate the account holder, would indicate that information. For the non-account holder purchasing a similar monetary instrument, a purchase application form that would have identification of the non-account holder and appropriate spaces to be filled in by that teller would be appropriate.

Digitized by Google

So, it is a simple type of form that we have in our mind, Congressman.

Mr. TORRES. Very good.

I believe I caught the tail end of your response to the chairman when he was relating to the question of structuring and whether in fact the structuring provisions now in the statutes are adequate. It was my sense that they weren't, from what you said and also from what Ms. Toensing said.

I happen to believe that the structuring provisions, as set forth in statutes, are not working in my area of the country.

Just today, as I mentioned in my earlier testimony and my opening statement, I have talked to FBI agents who have worked on a major case in Los Angeles, one case that began in 1987, and they found out that money laundering was being carried out at the rate of $30 million to $50 million per week in one case.

So, I want to simply state that I don't believe that the structuring provisions are working and that what you have said today, both of you, all of you here, is that they are inadequate. I believe that this hearing is a testimony to that.

Would I be correct in that? You are probably knowledgeable about that case. Am I stating the facts right here?

Mr. HILSHER. I am not knowledgeable about that particular case, Congressman. I don't think that I can agree with you 100 percent that the structuring provision is not working. I think it is working. It is working best in those areas where the banks are sensitized and looking for suspicious activity right below that threshold.

However, I don't think there is a provision that could be created which will totally eliminate the structuring of transactions. If you set a threshold, any threshold, somebody is going to go a dollar below it or $100 below it. It is a difficult problem.

I do believe that the section that you drafted will go a long way to deterring the person who doesn't want to be identified with the purchase of monetary instruments from walking in the door in the first place. I hope that is the case.

But to give a total—to give an F-minus to the structuring provision, I think, is inaccurate, because we do have sensitized banks out there that are making reports of suspicious, structured transactions. In fact, as I mention in my statement, the 45-ton seizure off the coast of San Francisco started because one teller had a $14,000 transaction, that when the customer determined that a report would have to be filed, he turned it into an $8,000 deposit with a follow-up $6,000 deposit the next day. That report of suspicious activity started the whole ball rolling.

So, I don't think we can [illegible] it a failure. I think it would be more accurate to say that we n[illegible] to continue to look for the fix that will make the overall act m[illegible] effective.

Mr. TORRES. My time is [illegible]pired. I want to thank you all for testifying toda[illegible]

The C[illegible]

Ms. [illegible] C[illegible]rm[illegible]. I want to add my appreciation [illegible]t hearings in our battle against [illegible]

Digitized by Google

I think we do well to heed the admonition of "follow the money," and you are giving us an opportunity today to receive some understanding of how the money does travel.

I am fascinated by the prospect that banks would tell the depositors or the borrowers of the interest of the Government in the transactions that they are making.

You said a big borrower is like an insider, almost, in certain respects. Does that mean in those particular banks involved, they lend big money to people who are like insiders or people who borrow big money become like insiders? What does that relate to?

Ms. TOENSING. It works both ways. I had an investigation when I was leaving Michigan where the whole financial institution was being run by dope dealers. And they not only had their insiders, but they had people that they were giving lots of money to. And we were caught because we couldn't subpoena any records because if we did that, we gave notice to everybody that we were investigating them.

Ms. PELOSI. That would be the exception?

Ms. TOENSING. Well, sometimes it is a very important case. The exception means that there is one more area where you can't go after somebody. It is a gaping hole.

Ms. PELOSI. It is enough of a consideration?

Ms. TOENSING. Yes.

Would you like to add something?

Mr. SAPHOS. All of us have had the same experience, I presume, in investigating financial institutions that were run by the bad guys or were so entwined with the business of the bad guys they could not afford to lose their business.

That is, of course, the minority of the financial institutions, and it is certainly a minority of bankers. But I investigated one financial institution that was essentially established for the purpose of servicing 10 money launderers, and in fact they didn't even identify them by name, they were just "1 through 10."

The reason they did that is because money launderers take so many counterfeit dollars that they would write on the wrapper for each of those persons whether that was money launderer 1 through 10 that turned in the money, so when they detected the counterfeit they would know whether they should debit that amount of money from 1, 4, 8, 9, or 10's bank account because they got so much money from these people every day and they got so many counterfeit bills from them every day.

In another situation I was investigating, a money launderer was going through a financial institution, and I called the chief of security for the institution personally, and I said, "I am going to serve a subpoena on you. It is very important that you don't notify the customer because I believe that you have got a corrupt branch. If there is anything in the subpoena that you cannot provide to me without telling the branch or letting the customer have some intimation of the investigation, don't comply with that portion of the subpoena. I will understand."

Two days later, as I recall, as the target was leaving the country for the last time, he said to a customs inspector, "I hear you subpoenaed my bank accounts." He has not returned to the United States since then.

Digitized by Google

Ms. TOENSING. Let me add, we have got the situations where here is the financial institution and we want the records or we know that there is something bad going on in there.

Here are our options: We can get a grand jury subpoena, which means that if we know that there are bad guys inside, we have given notice by the grand jury subpoena; or if we go by some other kind of—if there are not bad guys inside but if we go by some other process, some other legal process like an administrative proceeding, then the notice is given to the customers by law.

It is not that the banks want to or that they are in cahoots particularly. It is that the law requires it right now. And that is what we are asking to be changed. Or, if a regulatory agency sees fraud because they went in to get records or they were doing an audit, they cannot turn those records over to us without giving notice to the customer that these records are being turned over. That again is required by the law and what we are asking to be changed.

Ms. PELOSI. It sounds like we have several problems: the drug problem, the money laundering, and the conduct of certain banks which I would imagine is an infinitesimal percentage of the banks in the United States. So, as we address the problem, I hope we do not burden law-abiding banks.

As enthusiastic as I am to see this money laundering situation corrected, Mr. Chairman, it sounds like we have another problem about disreputable bankers. Is most of the money laundering coincidental with these banks which are not reputable, or is it a pervasive problem?

The CHAIRMAN. Ms. Pelosi——

Ms. PELOSI. My time is up?

The CHAIRMAN. No. Justice is taking—and I don't critique them for this, but they are here to testify on money laundering in the bill before us. But they are taking this opportunity to ask for further changes in the right for Financial Privacy Act to assist them to find other abuses, I believe over and beyond. In other words, fraud, and criminal activities that might not always be related to a part of money laundering.

Ms. TOENSING. I happen to have bank fraud cases under me, so that is—Mr. Saphos has all of the narcotics cases in his section. But one of my sections does all of the bank fraud cases, so I am acutely aware.

The CHAIRMAN. She has enormous jurisdictions. She is probably Justice's counterpart to the Energy and Commerce Committee.

Ms. PELOSI. My goodness. No greater compliment could anyone receive.

In any case, it sounds like a wonderful opportunity for us, and I appreciate your testimony, and that goes for all of our witnesses as well. Thank you.

Thank you, Mr. Chairman.

The CHAIRMAN. May I interject a question here. Staff has made a remark to me. Are there no conditions under which, if you have that suspicion that there is going to be somebody flee the country, you can get an order from the court that would allow you to delay notice for a certain period of time?

Mr. SAPHOS. Sir, we can get an order of the court directed to the banking institution which has been served with the grand jury sub-

Digitized by Google

poena telling the institution they are directed under power of contempt not to give notice to the customer whose records are being sought by the subpoena.

The CHAIRMAN. But the precondition is that it be under grand jury proceeding?

Mr. SAPHOS. Yes, sir, that is correct.

Additionally, we would have the authority to seek a search warrant and go into the bank and seize the documents pursuant to a search warrant. That is a rather vigorous action which generally, if the bank is not adversarial and there is no threat that the bank itself would destroy the documents, is not advised.

The CHAIRMAN. Thank you.

Mr. Parris?

Mr. PARRIS. Thank you, Mr. Chairman.

It has been suggested to us, ladies and gentleman, that under existing law it is already a crime to structure a currency transaction so as to evade the reporting requirements. The banks, as you have already testified, must report "suspicious transactions," with the use of criminal referral forms.

Now, do I understand that verified identification of the participant is the only real additional requirement under section 2 of this bill? Is that a correct statement?

Mr. HILSHER. I think that is the number one purpose. The bank could have every suspicion in the world about a non-account holder customer coming in the door, but when he leaves the door and the bank wants to report on that suspicious transaction, they don't know who to report on. It is "some white male, age 35, blond hair, blue eyes, who just walked out the door," and who we may not see again. The identification requirement would allow us to identify him.

The CHAIRMAN. Reading glasses and a Virginia accent. [Laughter.]

Mr. PARRIS. The only money I launder is when I forget and leave my wallet in my pants and throw it in the washing machine. [Laughter.]

The last sentence of section 2 provides, Mr. Hilsher, that the financial institutions will verify according to regulations ascribed by the Secretary of the Treasury. Can you tell us what you have in mind there? "Can I see your drivers license? What is your social security number," are those the kinds of things we are talking about?

Mr. HILSHER. Yes. We are talking about things like drivers licenses. If we are dealing with a foreign national, we may be talking about a passport identification number. We are not talking about anything exotic at all, any type of identification that would ordinarily be accepted in a banking transaction.

Mr. PARRIS. Thank you.

Just to follow up on the question of the chairman, you are receiving 7.2 million CTR reports per year, 600,000 a month. How many additional would you anticipate if this targeting thing under section 8 is imposed? Have you done a study about that?

Mr. HILSHER. No, sir, we have not done a study. [illegible] the section by itself is very limiting. It is very restri[illegible]very precise. It requires the determination first by [illegible]at

Digitized by Google

there is a reason to invoke this particular extra reporting requirement on a specific geographic location or on specific financial institutions.

Mr. PARRIS. I understand what the section does. Just give me a guess. You expect it to double? It would be 10 times as much, one and a half? Give me a guess.

Mr. HILSHER. I don't know the numbers, Congressman, but we would not expect those CTRs or those special reports to go to Detroit. Instead, they would go to the local law enforcement in that geographical area to look at because speed is of the essence in this situation. They would look at those reports. They would hit the streets and take care of a problem in that local area. So, we wouldn't be tasking the IRS Detroit data center.

Mr. PARRIS. So, you would not impact on the 7.2 million now, presumably?

Mr. HILSHER. No, sir.

Mr. PARRIS. It is difficult for us, at least for me, to figure out if you are going to send a million of these reports to the local authorities—100,000? 10?

Mr. HILSHER. Congressman, it is unknown because right now what I would expect is for several weeks, perhaps you would require a county, perhaps San Diego County, perhaps the northwest quadrant of San Diego County, then it may be 100,000 in a month's time. Then it may only be 20,000.

Mr. PARRIS. It is very difficult, at least for me, to try to legislate in the dark, Mr. Hilsher. You are going to send 100,000 transaction reports to somebody in San Diego. I will give you a little bet about what percentage of them are going to be followed up or even reviewed. If you are going to send 10, OK, I can understand that.

Mr. HILSHER. I think that my testimony, Congressman, I suggest that we don't know exactly what the utility of this provision is going to be, and I think we are going to have to walk up to it and see how it works.

Mr. PARRIS. The last question, ladies and gentlemen, is: Is it not correct that for money laundering purposes right now a check that is not in bearer form, that has a designated payee, is not a monetary instrument under the law for that purpose and, therefore, if I am a drug dealer and I take illegal monies from the sale of illicit substances and deposit it in an account in an insured financial institution in this country, and I can lawfully write a check to a designated payee on that money without impunity, without criminal transactions, so I can thereby take illicit money, if you will, and launder it in a private way by not using a monetary instrument?

Mr. HILSHER. That is what the current law allows, Congressman, unless you have a fictitious payee. But that is not in your hypothetical.

Mr. PARRIS. Or a bearer payable, an instrument payable the bearer would be a monetary instrument under the law, wouldn't it?

Mr. HILSHER. That would be a monetary instrument.

Mr. PARRIS. OK. So, does this legislation correct that problem?

Mr. BARNARD. How does he deposit the cash? When he takes the cash to be deposited, that's where they catch that transaction. It is not after he——

Digitized by Google

Mr. PARRIS. Presumably, if that is a suspicious transaction——

Mr. BARNARD. It's got to be if it's $10,000. They've got to record it.

Mr. PARRIS. That is the 600,000 reports we're getting every month right now.

The CHAIRMAN. The time of the gentleman has expired.

The Chair might observe that 600,000 reports from 14,000 banks, you're talking about 40 reports per month per bank. Therefore, if San Diego County—you can figure it out—how many banks would there be in San Diego or in the State of Virginia if we were to determine there is a lot happening in Virginia. Take the number of banks, multiply it by 40 on an average, and you ain't got that many reports that would be going to the local office.

Mr. PARRIS. The mathematics in Virginia are substantially different from those in Rhode Island, Mr. Chairman. If you take 600,000 and divide it by the number of banks, I don't think——

The CHAIRMAN. 14,000 into 600,000 would give you about 40.

Mr. PARRIS. I'm sorry. I misunderstood.

The CHAIRMAN. Per bank. We figure pretty well in Rhode Island. [Laughter.]

Ms. TOENSING. Let me point out on the question about the bearer and the cash. The person could be putting cash into his account at $6,000, $8,000, so it doesn't necessarily get covered in the going in.

Ms. RUDNICK. In addition, what we have done in connection with exemption booklet, we have surveyed the banks that have been filing CTRs to determine which banks are not using the exemption provisions. And we have found that the 50 largest banks in this country not using exemptions have accounted for 690,000 CTRs a year, and that is extrapolated from a 2-month period alone. So, that is about 1/10 of the CTRs that are being filed.

So, we are hopeful that once we get our exemption book out to the banks, you are going to see a dramatic reduction in the amount of unnecessary CTRs that are going to be filed.

The CHAIRMAN. Good observation.

Mr. Barnard?

Mr. BARNARD. Thank you, Mr. Chairman.

Mr. Chairman, I know how sensitive the Bank Secrecy Act is, especially to a lot of the senior members on this committee, because they were here when it was passed and there was good evidence of a need for that bill when it was passed, and there is still evidence of the need for the Bank Secrecy Act today.

But we have seen instances where it is working to the disadvantage or, I might say, to the advantage of those who seek to defraud banks and bank customers as well as launder money. For that reason, I would like to just assure Ms. Pelosi that we have evidence, especially in California where insiders, including the Mafia and others, have never—they are not in the ownership of banks, but by being large borrowers, they control the banks and they seem to follow bank management in some instances from bank to bank to bank.

When you seek to involve them in the defalcation, you will find that you cannot touch them because of the bank secrecy laws.

So, Mr. Chairman, I hope that we will give a lot of consideration to these two suggestions that the Treasury has made. I see the

Digitized by Google

problem not only in money laundering, but I have seen the problem through studies that our committee has done, which you have been kind enough to include some of our recommendations.

The CHAIRMAN. I think, Mr. Barnard, that if we look at the Empire S&L situation in Texas—let me ask our witnesses, if I may.

Mr. BARNARD. Sure. My time is your time. [Laughter.]

The CHAIRMAN. That is Rudy Vallee. That is New England, too.

In the Empire, that is where they were flipping, land flips, X number of times a day. Now, did that come to Justice's attention as a result of information conveyed to you from the Home Loan Bank Board or the Texas Banking Commissioner, or how did it come to you, do you recall?

Ms. TOENSING. I would have to go back and find that out. It has been around for so long now.

The CHAIRMAN. Wouldn't that be an example of the type of situation where you would want to be able to get that information as expeditiously as possible?

Ms. TOENSING. Yes. I am glad you pointed that out, Mr. Chairman, because it took a long time for that investigation. It took us about a year into it before we could even get a handle on that case. It happened to be in my fraud section, and I have now 10 attorneys, 10 out of 45 in Texas, working on that whole scheme in Dallas. So, it has taken up a lot of Department of Justice time.

But it has been so long and so drawn out that I cannot recall how it first came to me. I will find that out if you would like it for the record.

[A letter from Victoria Toensing with the referred to information can be found in the appendix.]

The CHAIRMAN. That might be helpful to your request for the amendment.

Doug?

Mr. BARNARD. Thank you, Mr. Chairman.

I would like to submit for the record today, Mr. Chairman, a statement which outlines my support for these two amendments that have been offered, because I feel that—

The CHAIRMAN. Would the gentleman like to have them placed immediately after the testimony of Justice?

If there is no objection.

[The prepared statement of Hon. Doug Barnard can be found in the appendix.]

The CHAIRMAN. Mr. Carper?

Mr. CARPER. Thank you, Mr. Chairman.

Let me yield to Mr. Torres, who has one additional question.

Mr. TORRES. Thank you, Mr. Carper, for yielding.

The legislation we are dealing with does not attempt to impugn the cooperation of those banks that have been most helpful in attempting to stem this very serious problem.

I know that today banks of that nature were cited. Bank of America was one that had been cooperating in this kind of a situation.

Mr. Hilsher, I understand that Treasury prefers to have some flexibility in determining the appropriate dollar amounts for transactions triggering these provisions. As you have indicated to me previously, your own documentation shows that most cash transac-

Digitized by Google

tions involving these particular money instruments are conducted in amounts of between $3,000 and $10,000.

What other dollar amounts might be appropriate, and why?

Mr. HILSHER. Congressman, it might be that we would be back before you in 1 year or 2 years from now saying that with the $3,000 limit we need authority to go down to $2,500 because the smurfs have gone below the $3,000 limit and we would be coming back asking for additional authorization.

The original—when the $3,000 number came up, that was a rather arbitrary number. However, we did, as you suggested, some research into the situation and found that between $3,000 and $10,000 was a significant range of where these monetary instruments fell.

However, our further analysis indicated that these smurfing activities can go as low as $700 postal money order purchases time and time again. It might be, if there was a reason to target a financial institution other than a bank, that we would want to go below our $3,000 number. I think we just need the flexibility.

But I think that the $3,000 number is one that we would—it is probably one we would consider very seriously as a beginning point.

Mr. TORRES. Thank you.

Thank you for yielding to me, Mr. Carper.

Mr. CARPER. I apologize for arriving late. I missed your testimony and have been sitting here trying to read and catch up and also listen to the questions and have not succeeded very well at either one.

Let me just ask this. It looks like your testimony, Mr. Hilsher, where you are talking about some recommendations to improve, I think, section 5325, could you just take a minute, you or anyone else on the panel who might wish to comment, and again just briefly, succinctly, state where and how can we further improve this measure when we mark it up?

Mr. HILSHER. When you go to markup on section 5325, it must be explicit to the financial institutions, that they have to provide the report of the identification to Treasury. Otherwise, they may just keep the report. But there is no requirement without a summons for us to get that information.

Second, as Congressman Torres indicated, we ask for flexibility in setting the monetary amounts so that we can do that by regulation and not come back to the committee. We can change more easily in that aspect.

Those are the only two major factors of 5325 that we would change.

Mr. CARPER. Anyone else on the panel? A recommendation for another change in the measure that we will be marking up? Do you like it just as it is?

Ms. TOENSING. We applaud and support Treasury.

Mr. CARPER. Good. Thank you.

Thank you, Mr. Chairman.

The CHAIRMAN. Let me get something clear on the flexibility you're looking for. Is that to do with the $3,000 amount?

Mr. HILSHER. Yes, Mr. Chairman.

Digitized by Google

The CHAIRMAN. But the flexibility, if we were to grant the flexibility, would you be satisfied if we were to say your flexibility goes not to increase the $3,000 or the $5,000, but to decrease it? Would that satisfy you? Would that be a happy compromise?

Mr. HILSHER. That would certainly be a compromise.

The CHAIRMAN. That would probably be easier to sell than total flexibility.

Mr. HILSHER. The one problem I have, Mr. Chairman, is that if we do target a large geographical region, not just a portion of San Diego County but all of Los Angeles County, we might be creating more work than we can handle at the $3,000 level. If I can do all of the banks in Los Angeles County at a $5,000 level and my agents can look at that where they couldn't look at all of those reports from $3,000 to $10,000, I am looking at improved field management.

I would be expecting the people in the joint currency task force or the financial investigations task force to tell me what level they are experiencing in the field in monetary instruments. They would know better than I. So, if they suggest $5,000 is a good number that they can work with, I would like to respond.

The CHAIRMAN. Suppose we were to try $3,000 with flexibility below that, to go lower if you want to, and let's see how it works?

If you have to up it, then you come back to us. It would be a simple thing. We would like to go to markup tomorrow.

Either that or—the last time in conference with the Senate, we sort of got rolled. I hope it doesn't happen this time. But I am just thinking of the fact that we do want to mark up tomorrow.

Mr. HILSHER. Mr. Chairman, I am reacting in some part to Congressman Parris' concern about too much work going into that local area.

The CHAIRMAN. I just gave you the numbers. And Ms. Rudnick just pointed out that numbers, even if you were to take the whole State of California, you wouldn't have that many. You know, and you're not going to go—and if you're talking of the geographic area, you're not going to target for 5 years, you're going to target for a limited period of time.

Is that not correct?

Mr. HILSHER. That is correct, Mr. Chairman.

Mr. SAPHOS. Sir, could I suggest respectfully that, in support of Mr. Hilsher, perhaps it would be inappropriate to put any amount at all one way or the other into the bill insomuch as it might well be sending a signal out to the money launderers.

The CHAIRMAN. Excuse me. Mr. Torres, who is very intimately involved in this section, could you please—I'm trying to have some help.

Mr. TORRES. I understand, Mr. Chairman.

The CHAIRMAN. If you would repeat that, Mr. Saphos.

Mr. SAPHOS. I would be concerned that, by putting any amount of money into the bill as a flat amount of money, we would send out a very distinct message to the money launderers that starting the day after tomorrow, $2,999 is OK.

Therefore, I think that perhaps the flexibility that Mr. Hilsher is looking for, by allowing the Secretary of the Treasury to supply the

Digitized by Google

money launderers in any particular geographic area in the midst of their activities, as a law enforcement function may be wise.

Now I certainly think, however, the recommendation which has been very strongly made by this committee that $3,000 is an extremely appropriate amount to look at, has been heeded by the law enforcement people.

I think they're going to take that home with them and not forget that.

But, perhaps putting it in black and white in the statute is a message to the money launderers and is not such a good idea.

The CHAIRMAN. I am told that $10,000 is also a flexible number, that Treasury could change that, lower it or increase it, if they wish.

So it could be that what we would do would be put $3,000 in but with the flexibility and in the Committee Reports strong language to the effect that it is the feeling that that is an appropriate number, and that it is up to the Secretary to determine if he wished to, or if she wished to exercise that flexibility, that it be done only with good cause.

We will consider that in our markup tomorrow.

I'm sorry. Mr. Wortley.

Mr. WORTLEY. Thank you, Mr. Chairman.

Ms. Rudnick, are you Stanky II?

Ms. RUDNICK. I think I'm actually Stanky III. There was one person in between us.

Mr. WORTLEY. Your predecessor was certainly one of the greatest authorities we had on the subject of money laundering. And we always appreciated having him come before this committee.

Now we are talking about lowering the threshold of reporting, and we're going from 10,000 down to 3,000, or some other arbitrary figure.

You are already getting some 600,000 reports——

The CHAIRMAN. Excuse me. Two different things. The CTR is 10,000. The 3,000 is for identification.

Mr. WORTLEY. Oh, the 3,000 is for identification.

Well, I did also notice though that, in 1986, when we had this subject before us, there was an indication that it was taking 2 months from the time the bank reported the transaction until it got to the necessary law enforcement agencies.

What is the situation on that now in Treasury?

Ms. RUDNICK. Right now, the banks have 15 days to file a report with Detroit. Detroit gets that information on line at the close——

Mr. WORTLEY. They mail it to Detroit?

Ms. RUDNICK. They mail it to Detroit, or they file magnetically. We made a permanent program on December 31, of magnetic filing. We have found as a result of that program that the information not only gets on to the IRS data base much more rapidly, but it is also more accurate because the financial institutions themselves are correcting the information.

Once it gets to Detroit, the close of the following business month, they have all of the transactions for the previous month on tape.

Tapes of those are then made available to Customs and in about 2 weeks, Customs has it on their TECS system but it is on line in Detroit 30 days after the close of the next month.

Digitized by Google

Not only can Customs use that IRS financial data base, but we at Treasury have on line access and we are working with the regulatory agencies to provide them with immediate on line access also.

Mr. WORTLEY. Are you telling me it is not taking 2 months for the law enforcement agency to get the necessary information?

Ms. RUDNICK. It would take between 1 and 2 months depending on what time of the month the CTR is filed.

Mr. WORTLEY. It is still a long, dragged out process. Is there any way of expediting it?

Ms. RUDNICK. The magnetic filing is the way to go. We have been encouraging banks to magnetic file. I believe now we have three financial institutions, one representing a very large holding company that is filing magnetically.

In the next several weeks, I believe Chase-Manhattan Bank and another bank will be filing magnetically.

I'm going to defer to Mr. Hilsher.

Mr. WORTLEY. What about the banks in southern Florida? Have they achieved this level of expertise yet?

Mr. HILSHER. The magnetic tape program just became a permanent program in December. I think there was a hesitancy during the pilot project phase for a lot of banks to invest the money and time to get into the project.

We are very encouraged that not only Chase Manhattan but Wells Fargo is anticipated to go into the program within the next month or so.

The time has gone down from 45 days from the date of the transaction before the CTR gets on the data base to 18 days under magnetic tape filing.

It is the way of the future. It also reduces the cost to the financial institution as well; that was also determined by the project. So we are hoping that the bottom line of the financial institution is going to cause those major filers to get on to the magtape program.

Mr. WORTLEY. I thank you very much.

Ms. Toensing, I have two questions, and I might get cut off because my time is running out.

One question is how many occasions have the regulators noted the appearance of money-laundering activities? Has it been a random thing? Or have there been a number of instances when we have had a failed bank?

In going through the records, they have noted considerable money-laundering activities.

And my second question to you would be—

Ms. TOENSING. Can we stop with that one? I'm not sure that I understand that. You talked about a failed bank. Are you talking about criminal activity within the bank, or only money laundering?

Because we have studied that, and we have determined that approximately 30 percent of the bank failures involve major criminal activity. How much of that is money laundering, we haven't broken that down.

Do you have it?

Mr. SAPHOS. I know——

Mr. WORTLEY. Thirty percent of the failures indicated criminal activity?

Ms. TOENSING. Yes, major criminal activity, which is even worse.

Digitized by Google

Mr. SAPHOS. Sir, we have not compiled those figures. We believe though, from our experience, there is an incidence that as a bank starts to go downhill it becomes more vulnerable to criminal laundering activities.

In order to test the theory which we have seen in a couple of instances, Mr. Hilsher and I have opened an office in Texas. We have given the instructions to our people there to look specifically at the failed or failing banks for the incidence of Mexican polydrug narcotics organizations laundering money through them.

Mr. WORTLEY. Very, very interesting.

May I throw in one more question, or is my time up?

The CHAIRMAN. Go ahead.

Mr. WORTLEY. Thank you, Mr. Chairman.

What evidence exists, Ms. Toensing, that nonbanking financial institutions, mutual funds insurance companies and the like, are being used, stock brokerage firms being used to launder money?

Ms. TOENSING. One is the recent E.F. Hutton indictment.

The CHAIRMAN. Providence, RI. Why did you have to bring it up?

Mr. WORTLEY. How could it happen in Providence, RI? [Laughter.]

You're just getting into that?

Ms. TOENSING. We're finding more and more cases in that area. And you're beginning to see them in the headlines.

Mr. WORTLEY. Have they existed, you think, for a while? They're just making the headlines now?

Ms. TOENSING. We're getting more people aware of reporting this. It is called raise your consciousness. A couple of years ago, no one even knew the word "smurf" and we're learning it daily, about this activity and really what is happening behind it. So people are getting concerned about it.

With that, we are getting more cooperation with law enforcement. And we are learning about these cases and learning how to investigate them.

Mr. WORTLEY. I think, in the last bill, in 1986, we kind of expanded the definitions of financial instruments, and things like insurance companies might be involved in, and perhaps brokerage firms fell into that new category.

Ms. TOENSING. I contend that one of the future ones is going to be the Indian reservations where we have unlimited gambling going on and we have not taken the measures necessary to limit the gambling or restrict it in certain ways.

Mr. WORTLEY. I have an Indian reservation in my congressional district. We will be on the alert.

Thank you, Mr. Chairman.

The CHAIRMAN. When you say 30 percent of bank failures, are you talking about 30 percent moneywise, or 30 percent of the actual institutions?

Ms. TOENSING. The institutions. In the institutions that fail.

The CHAIRMAN. The bulk of those are rather small institutions, comparatively speaking?

Ms. TOENSING. I would l e to look at those figures.

The CHAIRMAN. That h n my experience. As you know, I have been watching that closely. Oftentimes, it is the small-

Digitized by Google

er institutions that are used by the criminal element because they are easier to control.

Mr. Gonzalez.

Mr. GONZALEZ. I would interject a question. Since this is high-volume, 30 percent, how many indictments have been brought in?

Ms. TOENSING. On what?

Mr. GONZALEZ. On these institutions that evidence a pattern of criminal activity.

Mr. TOENSING. In other words, you're asking if there were major criminal activities in 30 percent of the banks, how many indictments?

I would have to go back and look at that because they wouldn't necessarily be bank fraud. It would be another section. It could have been money laundering, or it could have been a case where we couldn't pursue the criminal activity because all of the people had fled.

That would take a lot to get those statistics.

Mr. GONZALEZ. In Texas, for example, since Texas seems to be discussed, how many indictments have we had?

Ms. TOENSING. I think we have had 13 or 14 indictments of something like 19 or 20 individuals; all but one of the cases at this point that we have indicted has pleaded out or ended in a conviction. We have one that has not gone to trial yet.

But those statistics are changing weekly as we keep bringing more indictments. We are not through yet.

Mr. GONZALEZ. Thank you.

Ms. TOENSING. There is more to be done there.

The CHAIRMAN. Mr. McCollum.

Mr. MCCOLLUM. I don't have but one question, but I do want to commend you right off the bat for these proposals and whether or not this committee is able to adopt them, perhaps some of the committees working on the direct legislation will be able to.

I think they are excellent changes that have been proposed.

The question I have could apply to any of you. But, when we passed the changes back in 1986 to the Right of Financial Privacy law, one of the purposes of those changes was to encourage banks to volunteer information that they were previously afraid to volunteer for fear of being prosecuted.

I realize the act has only been in effect a short period of time. Do we have any evidence that those changes have brought about any help from the banks?

Ms. TOENSING. Yes. And as a result of some of these changes, we got together in the Department of Justice—actually, it preceded the changes a little bit, but I think we helped it long before, because we had this group called the Bank Working Group, and we put together the regulatory agencies overlooking financial institutions, with the FBI, the Department of Justice and some U.S. Attorneys' offices.

So we get that kind of thinking present. And their first project was to put together a referral form where the bank regulatory agencies could utilize this new kind of law and make references to us, giving us this minimal kind of information that we need, then to go back and ask for a grand jury subpoena.

Is Treasury working on that, on that working group?

Digitized by Google

Mr. HILSHER. No. We still have not been invited to participate in the Bank Fraud Working Group. [Laughter.]

Mr. MCCOLLUM. Let's get them going.

Mr. HILSHER. That was my suggestion, too.

Mr. MCCOLLUM. The bottom line is that banks are more willing to come forward than they were and help you identify.

Mr. Hilsher.

Mr. HILSHER. I would like to comment on that because we have seen a tremendous increase in the reports of suspicious transactions, some 300 referral forms relative to the Bank Secrecy Act from the FDIC and OCC that they receive from their banks.

I mentioned Bank of America with a suspicious transaction that resulted in this 45-ton hash-hish and marijuana seizure.

We have also—I believe the banks have really been sensitized as a result of the criminal enforcement, civil enforcement, and the activities of this committee heightened that awareness.

Many banks are coming forward looking for a new way. In fact, the Bank Administration Institute has a Subcommittee on Bank Secrecy Act Compliance. They are creating a subcommittee to look into reporting suspicious wire transfer activity.

Mr. MCCOLLUM. It is good to see some of the activity we do, as small as it sometimes seems to be, have some positive results.

Thank you, Mr. Chairman.

The CHAIRMAN. In other words, it is good to see the trees we planted bearing fruit.

I want to commend Ms. Rudnick for pitching in when it was time to pitch in. It was very helpful.

Mr. Hilsher, you were very wise to bring her along. I want to commend you.

We want to thank the panel. As I say, we are going to markup tomorrow and we will give every consideration to your requests, believe you me, as a result of our previous discussions and this hearing today.

The reason, incidentally, that we have a lot of Members not here is because this quorum precedes a very important vote. It has to do with how much pepper is going to be spread today around the Nation. Some day, I will tell you about the three Peppers. But, anyway, in this instance, it is Claude Pepper and the Pepper Bill. They called us to bring us to the floor to hear the concluding debate by the orators.

But I assure you that there is great interest by every Member of the committee because, as everyone knows, the drug problem is one of the foremost issues on the minds of everybody in public life today.

But it is most rewarding to know that we have such competent people as we have on this panel, and Mr. Wylie mentioned that as well, who are working in this area and who are so dedicated as well.

So we thank you for your testimony, for your answers to our questions, and for your very constructive suggestions that we shall certainly take into consideration and attempt to address as much as possible in tomorrow's markup.

Ms. TOENSING. Thank you.

The CHAIRMAN. The committee stands adjourned.

Digitized by Google

[Whereupon, at 3:56 p.m., the hearing was adjourned.]

Digitized by Google

APPENDIX

WEDNESDAY, JUNE 8, 1988

Digitized by Google

STATEMENT

OF

VICTORIA TOENSING
DEPUTY ASSISTANT ATTORNEY GENERAL
CRIMINAL DIVISION

BEFORE

THE

COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS
HOUSE OF REPRESENTATIVES

CONCERNING

LEGISLATIVE INITIATIVES TO PROTECT FINANCIAL INSTITUTIONS FROM DRUG TRAFFICKERS AND MONEY LAUNDERERS

ON

JUNE 8, 1988

Digitized by Google

Mr. Chairman and Members of the Committee, I am pleased to be here today to present the views of the Department of Justice on certain Committee initiatives intended to protect the country's financial institutions from being used by drug traffickers to launder money generated by their illegal enterprises. Before discussing several specific items, I want to express my gratitude and that of the entire Department of Justice for what the Committee has already accomplished in this area in just the last two years.

THE 1986 AMENDMENTS

In 1986, the 99th Congress passed and the President signed into law the Anti-Drug Abuse Act of 1986 (P.L. 99-570). Subtitle H of that Act was entitled the Money Laundering Control Act and contained the specific money laundering offenses set out at 18 U.S.C. 1956 and 1957. Equally important, it contained several provisions emanating from this Committee, particularly amendments to the Right to Financial Privacy Act (12 U.S.C. 3401 et seq.) and helpful changes in the Currency and Foreign Transactions Reporting Act (31 U.S.C. 5311 et seq.). For example, the Committee responded to the problem of money laundering by "smurfs" by adding a new section 31 U.S.C. 5324 to the CFTRA to prohibit the structuring of financial transactions to avoid the Act's reporting requirements.

The most significant change in the RFPA concerned expanding and clarifying rights of financial institutions to ensure that

Digitized by Google

information in their possession relevant to possible violations of law could be furnished to law enforcement authorities in a form maximizing the chances it could be used in an investigation. Specifically, 12 U.S.C. 3403(c) was revisad to state explicitly that if a financial institution had information which may be relevant to a possible violation of a statute or law that information could be furnished to a government authority. The amendment permits the financial institution to provide the name or other identifying information concerning any individual or account involved and the nature of the suspected activity. The 1986 amendment was intended to allow a financial institution to provide government officials with only enough information to permit the officials to obtain a subpoena, summons, or search warrant for additional information. It does not, however, permit disclosure of a customer's financial records.

The revised subsection also established a limited "good faith" defense in civil suits brought by customers against financial institutions that voluntarily disclose information under its provisions. Moreover, the subsection now preempts state and local privacy laws prohibiting voluntary disclosure of the information.

A. PROPOSED RFPA AMENDMENTS

Mr. Chairman, this nation is in the midst of a drug crisis. We are grateful for your past acts in helping to combat illicit money laundering -- the lifeblood of drug trafficking

Digitized by Google

enterprises. We solicit the Committee's aid again this year in making further statutory changes designed to facilitate law enforcement in waging a successful drug war, but which, at the same time, will not infringe upon the legitimate rights of law-abiding citizens.

Let me start with the RFPA. In brief, we are seeking changes in three areas:

(1) an exception to the RFPA for records involving possible crimes by financial institution "insiders," including major borrowers;

(2) relief from the notice requirements of the RFPA when financial records are transferred to the Department of Justice from another agency for investigation; and

(3) relief from a unique and burdensome requirement that financial records be physically presented to a federal grand jury.

(1) INSIDERS AND MAJOR BORROWERS

We join with the Committee in wanting to solve the problem of crimes by financial institution "insiders" -- officers, directors, employees, and controlling shareholders. As you know, the RFPA poses two major problems for law enforcement authorities in responding to insider abuses: first, RFPA prevents, even when criminal acts are suspected, disclosure of insiders' financial records to law enforcement authorities, and second, it requires that notice be given when such records are disclosed pursuant to

Digitized by Google

legal process. Thus, the RFPA serves as an insider's shield for crimes such as bank embezzlement and bank fraud.

Records that tend to reveal a violation of law by an insider should be turned over to government authorities for investigation without a notice alerting an insider that his or her crime has been discovered. Notice, of course, makes further investigation difficult, if not impossible. What is needed, therefore, is a specific provision in the RFPA stating the Act does not apply when a financial institution or supervisory agency provides to the appropriate government agency financial records of such insiders if there is reason to believe the records are relevant to a possible crime by the insiders against the financial institution or supervisory agency or in violation of the CFTRA or the money laundering provisions in sections 1956 and 1957 of title 18. Such a provision was contained in section 510 of H.R. 5484 which passed the House in the 99th Congress after being unanimously reported by this Committee. Unfortunately, the Senate failed to accept this provision in the Anti-Drug Abuse Act of 1986.

Inasmuch as the Committee is considering such an insider provision as part of its contribution to an anti-drug package being put together at the request of the Speaker, we think it is important the Committee include major borrowers, who frequently function in collaboration with institutional insiders.

One way to launder drug money is to use it to buy or make a down payment for a piece of real estate which can then be used as collateral for a loan. The drug trafficker/borrower then draws

Digitized by Google

on the loan which is a source of "clean" money that can be used for various purposes, including financing additional narcotics trafficking. Thus, we believe that including major borrowers (defined as those whose loans total at least a specific amount, such as $500,000) is an important aspect of this RFPA revision. If the Committee should decide not to include major borrowers per se in this exemption from the RFPA, it should strongly consider extending the exemption to major borrowers where there is reason to believe they may be acting in concert with insiders.

Moreover, this amendment of the RFPA should also amend 12 U.S.C. 3417(c) so that such a disclosure of financial records of insiders does not render the financial institution or an individual agent or employee thereof liable to the customer under State law. Without this provision, the exception to the RFPA would be worth very little since, in many instances, financial institutions would not turn over to federal agencies records indicating violations of federal law if to do so would render them civilly liable under state law.

Mr. Chairman, I have attached as an appendix to my statement a draft of how we think the above described insider/major borrower amendment to the RFPA should read. You may recall that we furnished it to you earlier this year after discussions between your staff and representatives of the Department. There are two other amendments to the RFPA which would be helpful and I would like briefly to describe them.

Digitized by Google

(2) NOTICE TO PUTATIVE DEFENDANTS ABOUT INVESTIGATIONS

The first concerns 12 U.S.C. 3412. That section presently provides that financial records obtained pursuant to the RFPA cannot be transferred from one agency or department to another without giving notice to the customer of the transfer. The notice-upon-transfer provisions apply even when the records are transferred to the Attorney General for use in a criminal investigation.

As you know, the Department of Justice has the responsibility for investigating most federal crimes and for prosecuting all of them. To do either of these two tasks we need to learn of the illegal activity. Obviously, we can do little about a crime -- even a major, ongoing enterprise like a drug importing operation -- if we cannot learn of it. And even if we do learn about it, the notice-upon-transfer provisions could serve to alert a criminal that his crimes have been discovered and give him or her an opportunity to flee or obstruct the investigation. Moreover, the notice provisions do little to advance legitimate privacy concerns since the records are already in the hands of one segment of the government which has a clear duty to notify the Attorney General of possible violations of federal law. Thus, the provisions of 12 U.S.C. 3412 act as an unjustifiable barrier tying the hands of the federal government in fully investigating and prosecuting criminal activity.

We need a limited exception to the provisions of 12 U.S.C. 3412 for situations in which an agency or department of the

Digitized by Google

federal government transfers records, obtained under the RFPA, to the Attorney General if the transferring agency or department has reason to believe the records may be relevant to a violation of federal criminal law. This exception would restore some balance between law enforcement interests and the legitimate privacy concerns recognized in section 3412. Such balancing of interests would be achieved if this exception is made applicable only if a supervisory official of the transferring agency or department certifies there is reason for belief that the records are relevant to a violation of federal criminal law, and mandates that the records may only be used for purposes of criminal investigation or prosecution and must be returned to the sending agency or department.

(3) PHYSICAL PRESENTATION OF VOLUMINOUS DOCUMENTS SUBPOENAED BY GRAND JURY

A final change in the RFPA would be helpful in cases involving huge volumes of records obtained by a grand jury subpoena. 12 U.S.C. 3420 requires that financial records about a customer obtained pursuant to such a subpoena must be returned and actually physically presented to the grand jury. No other law requires such a physical presentation. Testimony by an FBI agent summarizing the records has been held to be an inadequate "presentation." This unique requirement for presentation of documents to the grand jury is burdensome, costly, and serves no legitimate privacy interests since other provisions of the RFPA regarding

Digitized by Google

grand jury records and Rule 6 of the Federal Rules of Criminal Procedure adequately protect against unauthorized use of subpoenaed records. In at least three situations, the provision has required the convening of a grand jury in a storage location such as a warehouse under the control of the FBI away from the courthouse in order to "present" a large volume of bank records subpoenaed. Since recent budget constraints have limited grand juries in many districts to meeting only one or two days a month, spending time "viewing" cartons of records piled up in a storage warehouse is an unjustifiable waste of time.

This problem could be eliminated if the presentation requirement were modified by a provision stating that it can be dispensed with in cases where the volume of subpoenaed records makes the return and presentation impractical, in which case the grand jury would be provided with a description of the contents of the records.

B. PROPOSED CHANGES IN THE MONEY LAUNDERING STATUTES

Mr. Chairman, there are two amendments to the money laundering provisions in 18 U.S.C. 1956 and 1957 that federal investigators and prosecutors would find very beneficial. While I realize this Committee does not normally have jurisdiction over proposed amendments to title 18 sections, the ones I want to discuss are so closely related to areas under this Committee's responsibility that I would like to mention them briefly.

Digitized by Google

First, 18 U.S.C. 1956(a)(1) makes it an offense to conduct a financial transaction which "in fact" involves the proceeds of specified unlawful activity. The "in fact" language precludes use of government "sting" operations to investigate this offense. A sting operation would involve a government agent posing as a criminal -- a narcotics trafficker, for example -- and giving government money to a money launderer for the purpose of conducting a financial transaction. Such an investigative technique cannot be used because the money would not "in fact" be the proceeds of unlawful activity. This problem could be eliminated if the first paragraph of section 1956(a)(1) were amended to read:

> "Whoever, knowing that the property involved in a financial transaction represents the proceeds of some form of unlawful activity, or has been represented to be the proceeds of some form of unlawful activity, conducts or attempts to conduct a financial transaction which in fact involves the proceeds of specified unlawful activity or has been represented, directly or indirectly, to be the proceeds of unlawful activity --"

Finally, definitions in 18 U.S.C. 1956 and 1957 cover checks and money orders only if they are in bearer form. For purposes of section 1956, a "financial transaction" is defined as a transaction involving movement of funds by wire transfer or by "monetary instrument." "Monetary instrument," in turn, is defined as cash and various types of checks and money orders "in bearer form." Thus, if a drug dealer buys a boat with cash, he can be prosecuted under either section 1956 or 1957. But if he has previously deposited the cash into a checking account and writes out a check for the boat, neither statute reaches the transaction. This loophole could be closed by changing the

Digitized by Google

definition of monetary instrument in 18 U.S.C 1956(c)(5). A corresponding change should be made in the definition of a "monetary instrument" for purposes of section 1957 in subsection 1957(f). There the term is defined by cross reference to the Currency and Foreign Transactions Reporting Act. Subsection 1957(f) should be changed to refer to 1956(c)(5).

Mr. Chairman, that concludes my testimony and I would be happy to answer any questions the Committee may have.

Digitized by Google

APPENDIX

INSIDER AMENDMENT

FINANCIAL RECORDS OF INSIDERS.--(a) Section 1113 of the Right to Financial Privacy Act of 1978 (12 U.S.C. 3413) is amended by adding at the end thereof the following new subsection:

"(1) CRIMES AGAINST FINANCIAL INSTITUTIONS BY INSIDERS.--Nothing in this title shall apply when a financial institution or supervisory agency provides financial records of any officer, director, employee, major borrower (whose loans total $500,000 or more) or controlling shareholder (within the meaning of subparagraph (A) or (B) of section 2(a)(2) of the Bank Holding Company Act of 1956 or subparagraph (A) or (B) of section 408(a)(2) of the National Housing Act) of such institution to the Attorney General of the United States, to a State law enforcement agency, or, in the case of a possible violation of subchapter II of chapter 53 of title 31, United States Code, to the Secretary of the Treasury if there is reason to believe that such record is relevant to a possible violation by such individual of --

"(1) any law relating to crimes against financial institutions or supervisory agencies by directors, officers, employees, major borrowers or controlling shareholders of financial institutions; or

"(2) any provision of subchapter II of chapter 53 of title 31, United States Code.

Digitized by Google

(b) Section 1117(c) of the Right to Financial Privacy Act of 1978 (12 U.S.C. 3417(c)) is amended by striking out "Government authority shall not be liable to the customer for such disclosure" and inserting in lieu thereof "Government authority, any financial institution or agent or employee thereof making a good faith disclosure pursuant to section 3413(l) of this chapter, shall not be liable to the customer for such disclosure or for any failure to notify the customer of the disclosure under this chapter or any constitution, law, or regulation of any State or political subdivision thereof."

Digitized by Google

NO NOTICE UPON TRANSFER OF RECORDS AMENDMENT

TRANSFER BY GOVERNMENT AGENCY OF RECORDS TO DEPARTMENT OF JUSTICE FOR CRIMINAL INVESTIGATION. -- Section 1112 of the Right to Financial Privacy Act of 1978 (12 U.S.C. 3412) is amended by adding at the end thereof the following new subsection:

"(f) Nothing in this title shall apply when financial records obtained by an agency or department of the United States are disclosed or transferred to the Attorney General upon the certification by a supervisory level official of the transferring agency or department that there is reason to believe that the records may be relevant to a violation of federal criminal law. Records so transferred shall be used only for criminal investigative or prosecutive purposes by the Department of Justice and shall, upon completion of the investigation or prosecution (including any appeal), be returned only to the transferring agency or department.

AMENDMENT PERTAINING TO PRESENTATION TO GRAND JURY

EXCEPTION TO REQUIREMENT OF ACTUAL PRESENTATION OF FINANCIAL RECORDS TO GRAND JURY. -- Section 1120(1) of the Right to Financial Privacy Act of 1978 (12 U.S.C. 1120(1) is amended by inserting before the semicolon "unless the volume of such records makes such return and actual presentation impractical in which case the grand jury shall be provided with a description of the contents of the records".

Digitized by Google

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

For Release on Delivery
June 9, 1988

STATEMENT OF THE HONORABLE GERALD L. HILSHER
DEPUTY ASSISTANT SECRETARY (LAW ENFORCEMENT)
U.S. DEPARTMENT OF THE TREASURY
BEFORE THE
COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS
UNITED STATES HOUSE OF REPRESENTATIVES

June 8, 1988

Mr. Chairman and Members of the Committee:

I am pleased to have the opportunity to testify before the Committee today about the Committee's draft bill which would revise the Bank Secrecy Act and the Right to Financia Privacy Act. We understand that this bill will be put forward by the Committee for inclusion in the House Omnibus Drug legislation While the Department of the Treasury is generally in agreement with the Committee' bil we have comments that we hope you will consider carefully We also would like to discuss the legislative proposals with respect to the Bank Secrecy Act and related statutes that have been developed by Treasury under the auspices of the National Drug Policy Board These proposal will be forwarded to Congress very shortly Finally, would like to update the Committee on Treasury's activities in the area of financial and Bank Secrecy Act enforcement since our testimony last May.

Before I begin, I want to commend you, Mr. Chairman, and the Committee for your continued interest in effective administration and enforcement of the Bank Secrecy Act Over the years you and the Committee have played a vital role in making the inancia community aware of its responsibilities for full compliance with the Bank Secrecy Act and of the consequences of violating its requirements. You also have been most responsive when Treasury has sought to enact new legislation to enhance ts authority for ensuring compliance with the Bank Secrecy Act and to prevent money laundering activities.

B-1445

Digitized by Google

The Committee's bill sets forth two new Bank Secrecy Act provisions, 31 U.S.C. 5325 and 5326. First, I would like to discuss proposed section 325, which is aimed at one method of money laundering, specifically "smurfing," through the cash purchase of monetary instruments -- cashiers' checks, bank checks, travelers checks and money orders. This provision was drafted by Congressman Torres.

The intent of proposed Section 5325 is to require identification from money launderers who are not account holders at the financial institutions where they purchase monetary instruments with cash Under the Bank Secrecy Act, the only identification records currently required for individuals who do not engage in currency transactions in excess of $10,000 are those that pertain to new accounts Thus, under the Act, a customer who does not have an account relationship with a financial institution can engage in currency transactions under the 10 000 reporting threshold without being detected by the Government and, often, by the financial institution.

Proposed section 325 would require financial institutions to obtain identification and maintain a record of cash purchases of these monetary instruments by nonaccount holders To comply with this requirement Treasury envisions that financial institutions would need merely to maintain a chronological log of the cash purchases of these instruments. This log would be reported to Treasury upon request.

Treasury believes that the requirements of proposed Section 5325 will be a useful deterrent to the practice of smurfing through the purchase of monetary instruments and will not be overly burdensome for financial institutions In fact, Treasury has recommended that a proposal similar to Congressman Torres proposal be included in the Administration's recommended legislative proposals being developed in the National Drug Policy Board.

Treasury does, however, have some recommendations that we believe would improve section 5325. First, we recommend that Treasury's authority to require the financial institution to provide Treasury with a report of the identification information it has obtained be made explicit in the statute Second we urge the

Committee to delete any reference to a specific dollar amount at which the identification information would be required from the statute. Rather, we would prefer for the Secretary of the Treasury to be given the authority to determine an appropriate amount by regulation. In this way, Treasury will be able to respond more easily to changing law enforcement needs.

Digitized by Google

Under the second proposed provision, section 5326, the Secretary of the Treasury would be able to issue an order to target financial institutions in certain geographic locations for special reporting of currency or monetary instrument transactions in an amount less than $10,000 for a limited period of time. The location would be selected based upon a determination by the Secretary that there may exist a high level of drug money laundering activity in that area. A request from a Treasury law enforcement "currency group" or joint financial investigative task force would trigger such a determination.

Under this proposal, Treasury would be able to require all financial institutions to file currency reports at an amount lower than the normal $10,000 reporting threshold under the Bank Secrecy Act. The purchasers of these instruments would have to provide the identification required under the Bank Secrecy Act. Treasury envisions that the form to be used for making these reports would be the Currency Transaction Report ("CTR") which is filed on Form 89, and that no new form would be developed. The report then would be separated from the usual CTRs and analyzed by a team of Treasury investigators or analysts working in the currency group or in a joint financial task force in the targeted location.

Because time would be of the essence in maximizing the utility of the information obtained pursuant to a targeting order, Treasury is pleased to see that the bill exempts any order issued pursuant to proposed section 5326 from the normal delayed effective date provisions required for regulations under the Administrative Procedure Act ("APA").

The implementation of a request to target a limited geographic area does present some practical problems for Treasury as well as the affected financial institutions. First, Treasury would have the responsibility for quickly identifying all the financial institutions to be targeted in the specific geographical area. While would not be difficult for Treasury to identify the affected banks, it would be difficult for Treasury to identify certain categories of nonbank financial institutions, e.g. currency exchanges and check cashers. Second, Treasury would have to transmit notice of the order by letter to all the affected institutions. Finally, the targeted institutions would have to educate their tellers and other employees very quickly, as to the new reporting requirements and any additional recordkeeping procedures.

Despite the practical difficulties in implementing any order, Treasury believes that the information obtained could be highly useful to law enforcement officials. On-the-spot analysis of the information may very well lead to the breakup of money laundering organizations. For this reason, Treasury is anxious to develop and refine the concept. Treasury recognizes, however, that a

Digitized by Google

significant drawback to any approach that is limited geographically will result in driving money launderers on to new locations where law enforcement officials and financial institutions may not be as sensitive to patterns of money laundering.

While we cannot judge with certainty the outcome of this kind of targeting, Treasury hopes that next year, we will be able to come back and report favorably to the Committee on its utility.

In addition to the amendments to the Bank Secrecy Act contained in the Committee's bill Treasury hopes that you will consider including a number of technical corrections to the Money Laundering Control Act of 1986, Subtitle H of the Anti-Drug Abuse Act of 1986, Pub. L. 99-570, in the bill.

First, 31 U.S.C. 5312 needs to be amended to correct a numbering error. As you know, that provision sets forth a list of the types of financial institutions subject to the Bank Secrecy Act. When the Postal Service was added to the list of financial institutions in the Money Laundering Control Act of 198-, a numbering error resulted. This error needs to be corrected.

Another technical correction relating to the Postal Service is also necessary. When the Postal Service was added to the list of institutions subject to the Bank Secrecy Act, no corresponding change was made to U.S.C. 5318(a). That section currently authorizes the Secretary of the Treasury to delegate enforcement responsibility for Bank Secrecy Act compliance only to "supervising agencies." Because the Postal Inspection Service, as part of the Postal Service, cannot be considered a supervising agency under current law, the Secretary may not delegate enforcement authority for Bank Secrecy Act compliance by the Postal Service to the Postal Inspection Service. Therefore, an amendment is needed to add the Postal Inspection Service to the list of agencies to which Treasury can delegate enforcement authority.

The bill also should be modified to correct an inadvertent omission that arose in connection with the 986 revision to the civil penalty provision for violations by financial institutions of the reporting requirements of the Bank Secrecy Act, U C. 5321(a). As you recall, in the 986 Act, the amount of a civil penalty that could be assessed against a financial institution for reporting violations was raised to an amount keyed to the underlying unreported funds. At the same time, however the daily penalty for violations by financial institutions of procedures promulgated by Treasury under 31 U.S C. 5318 was inadvertently dropped. The bill should be modified to reinsert the daily penalty of $10,000 for violations of procedures.

Digitized by Google

There is also a critical need for revision to the recordkeeping provisions of the Bank Secrecy Act, 12 U S.C 1829(b) (applicable to insured banks), and 12 U.S.C. 1951-1959 (applicable to nonbank financial institutions). Violations of the recordkeeping provisions of the Bank Secrecy Act can be as deleterious to law enforcement as violations of the reporting provisions

Nevertheless, there is currently no civil penalty applicable to insured banks which violate the recordkeeping provisions. There should be a civil penalty for both willful violations of the recordkeeping provisions up to a maximum of $1 000 and a maximum $500 penalty for negligent violations of these provisions by these institutions. Also, the pena ty applicable to nonbank financial institutions subject to the Bank Secrecy Act for recordkeeping violations should be raised from a maximum of $1,000 per violation to $2w,000 per violation and a $500 negligent penalty added. The definition of nonbank financial institutions subject to the penalty also should be amended to cover all types of nonbank financial institutions under the Bank Secrecy Act. At this time, institutions such as casinos are not covered.

Although not within thi Committee's jurisdiction, but certainly of interest to the Committee would be Treasury's recommendation to revise the Internal Revenue Code to complement Treasury's Bank Secrecy Act authority This revision would provide all law enforcement officials and not only the IRS, with access to reports filed under section 6050I of the Internal Revenue Code.

Section 6050I, which is similar to Section 313 of the Bank Secrecy Act, requires cash reporting of amounts in excess of $10,000 received in "trades or businesses" other than those covered by the Bank Secrecy Act. Clearly these reports are, in many instances, of comparable utility to law enforcement, especially in drug cases, e.g., reports on the cash purchase of motor vehicles or real estate. Unfortunately, however, the IRS disclosure restrictions in Internal Revenue Code section 6103 currently do not allow analysis of the information or law enforcement access on a par with Bank Secrecy Act information.

Treasury strongly recommends that an amendment be made to section 6050I to exempt returns filed under that provision from the disclosure restrictions of section 103. This will enable law enforcement to analyze section 6050I returns with Bank Secrecy Act reports as part of Treasury's financial data base and permit Treasury to disseminate these reports to law enforcement agencies to the same extent as Bank Secrecy Act reports Enforcement responsibility for section 050I would remain with IRS. Section 6050I reports (like Bank Secrecy Act reports) would be exempt from the Freedom of Information Act.

Digitized by Google

Finally, we recommend that an anti-structuring provision be added to section 6050I that is comparable to the Bank Secrecy Act anti-structuring provision applicable to customers who structure transactions to evade the Bank Secrecy Act reporting requirements, 31 U S.C 324, and that a willful violation of section 6050I be punished as a felony offense, and not just a misdemeanor. This proposal has been suggested for inclusion in the National Drug Policy Board legislative proposals.

I would like to turn now to the Committee's proposed amendments to the Right to Financial Privacy Act ("RFPA"). While Treasury shares the Committee concerns with protecting the financial privacy of individuals Treasury believes that in today's climate, we must, in imited areas, reevaluate the appropriate balance between the right to financial privacy and the legitimate needs of Federal law enforcement. Treasury remains sensitive to protecting the privacy rights of individuals within the context of law enforcement.

Treasury, therefore, is very pleased that the bill does include a revision to the RFPA that would allow information and records relating to possible crimes against financial institutions or against supervisory agencies by insiders to be provided by the financial institution or supervisory agency to the Department of Justice without notice to the insider As you are well aware, prior notice would enable the alleged wrongdoer to transfer assets or otherwise impede the investigation As Treasury has testified before the Committee, we firmly agree with you on the need for this measure

While the draft bil similarly provides that possible violations by insiders of the Bank Secrecy Act may be reported by a financial institution or supervisory agency to the Secretary of the Treasury without notice, Treasury would like to point out that, at least with respect to officers directors and employees, existing law already clearly authorizes such disclosures This is because, under section 1101(6 H) of the RFPA, Treasury is a supervisory agency for purposes of Bank Secrecy Act enforcement. Section 1113(b) sets forth that "[n]othing in this chapter [RFPA] prohibits . disclosure to any supervisory agency of financial records or information in the exercise of supervisory regulatory or monetary functions with respect to a financial institution. Under delegations from Treasury, bank supervisory agencies routinely examine institutions and report to Treasury possible Bank Secrecy Act violations by financial institution officers, directors and employees and provide supporting financial records where necessary. without notice. Financial institutions also disclose information and records about their own past noncompliance to Treasury without reference to the RFPA. We strongly urge you to emphasize in the Committee report that this is not a change to existing law.

Digitized by Google

Unfortunately, the law is not as clear, and an amendment to the RFPA is very much needed, to permit financial institutions to report possible violations of the Bank Secrecy Act by their customers, i.e. in situations where the bank suspects that its customer has violated 31 U S.C 5324, the anti-structuring provision of the Bank Secrecy Act. If the bank is not implicated in the possible anti-structuring violation, broad disclosure to Treasury arguably may not be within the exercise of Treasury's "supervisory functions .. with respect to a financial institution." Banks then only would be able to provide Treasury with the limited suspicious transaction information allowed by section 1103(c) of the RFPA.

Generally, without access to the underlying customer account records and other information about the customer, this limited information would not be adequate to establish probable cause that the anti-structuring provisions of the Act have been violated. Without probable cause, Treasury cannot proceed to seize funds that are on deposit with financial institutions. Instead, Treasury would have to issue a summons to the institution for the account records and other information and provide notice of the summons to the customer Notice to the customer would be fatal to the investigation and seizure action, because once the customer has knowledge of the summons, he can withdraw the money on deposit or wire transfer it to a foreign jurisdiction.

For these reasons, we would urge you to include a provision in the RFPA that would allow a financial institution to report, in good faith, all available information and to disclose records with respect to possible violations of the Bank Secrecy Act by customers without notice to the customer and without fear of civil liability.

If an amendment to the RFPA is made which permits financial institutions to disclose information without customer notice, it is imperative that a corresponding amendment be made that protects a financial institution from civil liability to the customer under State law if the disclosure is made in good faith. Without this federal preemption, financial institutions will be faced with the possibility of civil liability under State financial privacy laws, and they will be deterred from cooperating with law enforcement. As I will discuss later in this statement, cooperation from the financial community in reporting suspicious transactions is an increasingly important aspect in the attack against the financial infrastructure that supports the drug trade.

There is one technical amendment that is needed to the RFPA. When Congress amended the suspicious transaction provision, section 1103(c), in the 1986 Act, to specify what information a financial institution could give relating to possible violations of law or regulation, a good faith preemption clause was included.

Digitized by Google

However, an ambiguity was created about whether financial institutions are protected from liability for good faith reports of possible violations of law or regulation when the violations involve corporations or corporate accounts. Although the legislative history makes it clear that Congress contemplated that situations involving corporations would be covered, the RFPA itself does not apply to corporate privacy. See Sen. Rep. No. 894, 99th Cong., 2d Sess. 15-16 (1986). A reference needs to be made in section 1103(c) to expressly cover corporations. We have provided the Committee staff with draft language to this effect.

The Bank Secrecy Act Requirements and Enforcement Organization

Before I proceed to update the Committee on Treasury' initiatives in the area of Bank Secrecy Act and financial enforcement, I would like to explain briefly by way of background, what the Bank Secrecy Act is and Treasury's enforcement role in the area of Bank Secrecy Act and related financial enforcement matters.

As you know, the Bank Secrecy Act was enacted in 1970 and gives the Department of the Treasury broad authority to require the maintenance of records and the filing of reports that have been determined to have a high degree of usefulness in criminal, tax, or regulatory investigations or proceedings. In passing the Bank Secrecy Act, Congress hoped to lessen the impediment to U.S. law enforcement authorities posed by stringent foreign bank secrecy laws. Congress also hoped that the reporting of the sources, volumes, and movements of domestic and international currency would betray a wide variety of criminal activity, including drug trafficking and tax evasion. These hopes have been borne out.

The authority given to Treasury in the Bank Secrecy Act is generally not self-executing, but must be implemented by regulations promulgated by the Secretary in his discretion. Since the inception of the Bank Secrecy Act, Treasury in exercising this regulatory authority, has been acutely concerned with striking the appropriate balance between the needs of the law enforcement agencies and the costs of compliance to the financial community.

With this in mind, Treasury has imposed three major reporting requirements under the Act. Briefly, these reports are:

(1) The Currency Transaction Report (CTR) -- This requires that designated types of financial institutions report all types of cash transactions by, through or to the institutions in excess of $10,000. Financial institutions subject to this requirement include banks, savings and loans, credit unions, securities brokers and dealers, foreign currency brokers and several categories of miscellaneous financial institutions such as casinos, check cashers and currency exchanges.

Digitized by Google

(2) The Currency or Monetary Instrument Report (CMIR) -- This requires that all persons report the import or export of currency or monetary instruments in excess of $10,000 into or out of the United States.

(3) The Foreign Bank Account Report (FBAR) -- This requires that all persons subject to the jurisdiction of the United States make an annual report of their interests in foreign bank accounts

Finally, the Act and the regulations require financial institutions to maintain a variety of records (such as copies of signature cards, bank statements, and checks drawn for more than $100) for a five-year period. Records required to be kept under the Bank Secrecy Act, unlike the Bank Secrecy Act reports, generally may be examined by law enforcement authorities only for the purpose of assuring compliance with the Act's requirements; in other cases, authorities must obtain subpoenas or comply with other legal provisions As I discussed above in connection with the need for recordkeeping penalties the recordkeeping provisions, less well known than the reporting provisions, are of great value to law enforcement in the creation of a "paper trail."

The Secretary of the Treasury has delegated to the Assistant Secretary (Enforcement) overall responsibility for Bank Secrecy Act enforcement. Within my office, the responsibility for coordination of Bank Secrecy Act enforcement and policymaking rests with the Office of Financial Enforcement. That office is also responsible for imposition of civil penalties under the Bank Secrecy Act, which I will discuss shortly.

Enforcement is accomplished through a complex series of delegations emanating from and supervised by my office which I will briefly describe:

- The IRS Currency and Banking Reports Division is responsible for the computerization of the CTRs and FBARs. The IRS Examination Division is responsible for compliance examination of miscellaneous financial institutions for which examination authority has not otherwise been delegated.

- The IRS Criminal Investigation Division ("IRS-CID") is responsible for the investigation of all criminal cases (except CMIR cases) under the Bank Secrecy Act for all types of financial institutions

- The United States Customs Service is responsible for the computerization of the CMIRs and for civil and criminal enforcement of the CMIR provisions. In addition, Customs also maintains the combined data base

Digitized by Google

for all Bank Secrecy Act information. The Customs Financial Intelligence Branch is responsible for the analysis and dissemination of Bank Secrecy Act data for a variety of law enforcement purposes

- Examination of Bank Secrecy Act compliance is generally delegated to the various regulatory agencies that have responsibility for supervising financial institutions. The Office of the Comptroller of the Currency is responsible for the examination of national banks, the Federal Reserve System for State member banks the Federal Home Loan Bank Board for insured savings and loans, the National Credit Union Administration for Federal and Federally insured credit unions, the Federal Deposit Insurance Corporation for State banks that are not members of the Federal Reserve, and the Securities and Exchange Commission for federally regulated brokers and dealers.

Enforcement of the Bank Secrecy Act

Treasury views the Bank Secrecy Act as a law enforcement "tool," and enforcement of its provisions as the "grinding wheel that sharpens the tool. Thus, in the past three years, Treasury has been more vigorous than ever before in initiating investigations and levying civil penalties against financial institutions for civil violations of the Bank Secrecy Act. Since June, 198-, Treasury has levied civil penalties totalling over $16 million for Bank Secrecy Act violations in thirty-nine cases involving financial institutions. In a number of these cases, the civil penalty was assessed against bank holding companies that owned more than one bank that had violations Thus, these thirty-nine penalties actually involved one hundred and seven banks that Treasury concluded had violated the Act. Moreover, twenty-nine of these penalties exceeded $100,000 -- an indication that the violations to which the penalties pertained were neither isolated nor infrequent

In addition, in the past five years, IRS-CID has steadily increased the number of investigations and prosecutions for criminal violations of the Bank Secrecy Act. The number of indictments have increased from 29 in 1982 to 236 in 1987, and convictions have also increased from 25 to 153 during that same time period.

Another aspect of Bank Secrecy Act enforcement that is sometimes overlooked, but is no less vital for an effective compliance program, is the commitment of the United States Customs Service to enforcement of the Bank Secrecy Act requirements for CMIRs. During Fiscal Year 1987, Customs conducted a total of 2,138 seizures of currency and monetary instruments totalling $192,382,985 for violations of CMIR requirements Through April, in Fiscal Year 198 , Customs has conducted a total of 641 seizures totalling $56,323,737, for violations of the CMIR requirements.

Digitized by Google

The Financial Database

The CTRs CTRCs, and the FBARs are filed with the Internal Revenue Service and placed on a computer at the IRS Detroit Data Center. The CMIR reports are filed with the U S. Customs Service and are processed in Newington, Virginia. These reports when combined, form what we call the Treasury Financial Database. The Financial Database s accessible to Customs and IRS agents and financial analysts for targeting suspicious currency transactions, investigative case support, tax examination and collection, and a host of other law enforcement uses.

Both Customs and the IRS have rule-based, artificial intelligence ("A-I") systems massaging the data contained in the financial database, along with data received from the field. These A-I systems are based on rules of suspicious indicators, for instance, persons whose many CTRs list differing occupations, social security numbers, and addresses, and whose transactions involve multiple accounts or transactions at a variety of financial institutions. According to the expert rules used by the A-I system, certain occupations are more suspicious than others, and those that are more suspect are measured against the frequency and amounts of financial transactions. CTRs filed by financial institutions for amounts below the 10 00 report threshold, e.g. a $9 900 CTR, are considered suspicious by the A-I computer, because we have learned from experience that financial institutions often file such reports because they believe the currency transactions to be suspicious.

The A-I computer applies these and other rules against the database automatically and highlights certain "targets" for further analysis by human financial intelligence analysts, and ultimately for referral to the field for further investigation. To date, over 270 targets representing reportable CTR activity exceeding $201.9 million and reportable CMIR activity exceeding $21.6 million have been generated by the A-I systems.

The Treasury Financial Database also can be used for law enforcement purposes unrelated to tracking suspicious financial transactions Project Warrant is an operation being conducted through the Customs Financial Intelligence Branch which seeks to match information on fugitives against the database in the hope of locating escapees. persons under indictment. or persons for whom an arrest warrant has been issued. One notable success story for Project Warrant was the arrest, in November of 1987 of an escaped convicted murderer who had been a fugitive since 1984. The leads provided to the State police from the financial activity identified in the Project Warrant report culminated in the subject's arrest at the residence of one of his children. The address was obtained from a CTR filed in 1984 when the subject conducted a financial transaction.

Digitized by Google

We have been asked by many in the financial community and by Congress, "Doe anyone even look at the information that we send to Detroit?" hope you can see now that we do, and furthermore, how very important it is that the identity of the customer of a financial institution be verified and that the CTR be filled in completely including the occupation and address blanks.

Utility of Bank Secrecy Act

Now that have described how the financial intelligence divisions of IRS and Customs review and analyze this information, I would like to describe how these reports have proved highly useful for civil and criminal law enforcement purposes. Particularly in recent years, these reports have provided law enforcement authorities with investigative leads, information that corroborates other sources of information about criminal activities, and probative evidence in Federal criminal cases. Perhaps the most prominent example of the reports' utility can be found in United States v. Badalamenti (also known informally as the "Pizza Connection" case). That case involved the smuggling of substantial quantities of heroin into the United States by members of Italian and U.S. organized criminal groups. In the course of their investigation of heroin trafficking, Federal authorities discovered a number of CTRs that reflected large cash transactions by a Swiss national with stockbrokers in New York. These reports eventually led to the discovery of an extensive money-laundering operation that involved the transfer of tens of millions of dollars through investment houses and banks in New York City to financial institutions in Switzerland and Italy

Ultimately, twenty individuals involved in the heroin network and money laundering enterprise were convicted in Federal court on various charges, including heroin trafficking, conspiracy, racketeering and Bank Secrecy Act violation All received prison sentences ranging from fifteen to forty-five years. In addition, the Swiss national was convicted and imprisoned by Swiss authorities for violations of Swiss law relating to his money laundering activities.

The Government also has made substantial use of the Bank Secrecy Act to prosecute a number of leading money launderers in the United States and abroad. In recent years, for example, the Government has successfully prosecuted Isaac Kattan-Kassin, whose money laundering organization handled gross proceeds estimated at $200 million to $250 million per year; Ramon Milian-Rodriguez who transported approximately $146 million in cash from the United States to Panama over a nine-month period; Eduardo Orozco, whose money laundering organization laundered more than $15 million over a four-year period; and Barbara Mouzin, who master-minded and operated a large West Coast money laundering business for cocaine traffickers.

Digitized by Google

In some instances, even a single CTR can provide significant investigative leads for criminal investigators. In one case, the Internal Revenue Service analyzed a single CTR and determined that the individual listed on the CTR had not filed a tax return. Subsequent investigation disclosed the existence of a massive heroin distribution and money laundering organization, operating primarily throughout southern California, which provided false information to the financial institutions that filed CTRs on their transactions. Eventually, the IRS arrested more than a dozen persons associated with the organization, seized in excess of $2 million in currency at various domestic banks, and charged the organization with income tax evasion involving $27 million in income over a three-year period.

Although many of the examples cited above involved large-scale money laundering for drug traffickers, Bank Secrecy Act reports are also highly useful in identifying or proving other types of financial crimes, for instance, bank fraud and embezzlement. In one recent case for example analysis of reports filed by a bank provided a number of leads as to the disposition of tens of millions of dollars that had been embezzled from the bank through such devices as illegal loans. In another recent case Federal investigators discovered that a husband and wife had failed to file a CMIR form for the $1 ,00 in cash that they took out of the United States Further investigation determined that the wife had embez led millions of dollars from the savings and loan association in Texas at which she had been employed.

These examples amply demonstrate the substantial utility of Bank Secrecy Act reports. In addition unlike grand jury subpoenas or court orders, the reports provide a constant stream of data on large domestic and international movements of cash and ensures that law enforcement agents obtain valuable information on suspicious transactions in a timely fashion.

Suspicious Transaction Reporting

Treasury, and know that this Committee, expects more from financial institutions than mere compliance with the Bank Secrecy Act. We expect vigilance on the part of financial institutions to make timely reports of suspicious transactions. As you have heard us say many times, Treasury needs legitimate financial institutions to be partners with Federal law enforcement. Our message on this score has had very gratifying results with many banks and some securities broker Suspicious transaction reports have experienced a great upsurge in the last year In addition, banks regulated by the Office of the Comptroller of the Currency and the Federal Deposit Insurance Corporation have filed almost 300 Criminal Referral Forms or Reports of Apparent Crime.

Digitized by Google

A case in point that you have read about recently was the record-breaking drug seizure of 45 tons of marijuana and hashish on the barge Intrepid in San Francisco Bay. The seizure was a direct result of referrals of suspicious transactions to the Internal Revenue Service by the Bank of America and other banks. These reports prompted the Northwest Organized Crime Drug Enforcement Task Force to commence an investigation that led to the seizure of the barge.

This case commenced when, on August 7, 1987, an unidentified man entered the North Napa Branch of the Bank of America and tried to deposit $12 000 in cash into the account of a Napa Valley mortgage institution. Bank officials explained that under the Federal 98 Money Laundering Control Act, financial institutions are required to report any single deposit of $10,000 or more to the IRS. The man then reduced the amount of the deposit to $8,000 so that the report need not be filed. Later that day, the same individual returned with a check for $4,000 from another financial institution and deposited t into the Napa Valley Mortgage account. These events led the bank officials to believe that the individual may have been attempting to circumvent the reporting law They then called the IRS.

The rest, as they say, is history--a record seizure resulting from this tip. In addition to the drug seizure, at least six individuals have been arrested and over million in cash, three vessels and real property, have been seized I would like to take this opportunity to publicly thank the Bank of America and all of the financial institutions that are supporting the Treasury Department in its attack on the money that supports this insidious crime.

This is a stellar example of what can happen when financial institutions act in concert with law enforcement. Treasury actively encourages and depends on this type of cooperation. In order to facilitate this cooperation, within the next two weeks Treasury will be introducing, in conjunction with the Internal Revenue Service, a toll-free suspicious transaction number, 1-800-BSA-CTRS Financial institutions will be able to call this number to report possible Bank Secrecy Act violations or money laundering violations, within the confines of the RFPA. A similar toll-free number for Customs, 1-800-BE ALERT, for reporting possible CMIR and other Customs law violations has been operational for some time

Update on Treasury's Administration and Enforcement of the Bank Secrecy Act

Since last October Treasury has reorganized the Office of Financial Enforcement to increase its ability to act expeditiously on civil penalty cases The Office now has a new Director, Amy G. Rudnick, as well as a permanent Deputy Director, an Assistant

Digitized by Google

for International Affairs, an Assistant for Bank Secrecy Act Compliance on detail from the Office of the Comptroller of the Currency, a Compliance Research Analyst, and a Legal Intern. In addition, we have announced five additional permanent professional staff positions (one Bank Secrecy Act Compliance Supervisor, two Bank Secrecy Act Compliance Specialists and two Assistants for Legislation, Regulations, and Interpretations) to carry out the responsibilities of the Office. Treasury also has instituted a program where personnel from the various agencies with Bank Secrecy Act enforcement responsibility are working in the Office of Financial Enforcement on forty-five to one-hundred-eighty-day details. Currently, we have one detail from the Federal Reserve and one detail from RS/Examination Division The Federal Home Loan Bank System has committed a detai to begin on September 1988 We believe that these details will be mutually beneficial to Treasury and the regulatory agencies.

In addition, Treasury has been engaged in an extended project, through the Bank Secrecy Act Working Group that Treasury heads, to revise and expand the guidelines that the bank supervisory agencies follow in referring possible violations of the Bank Secrecy Act to Treasury. These revised guidelines, which have been adopted by most of the bank supervisory agencies, address a broader range of factors that the supervisory agencies should consider in deciding whether to make referrals in particular cases. They also seek to streamline the referral process to minimize the time that it takes to forward a Bank Secrecy Act referral from the district office of a supervisory agency to Treasury.

Treasury also has taken a number of administrative actions to make the Treasury Financial Database, in which computerized data from the Bank Secrecy Act reports are stored, more readily accessible to law enforcement and supervisory agencies. The Office of Financial Enforcement has had "on-line" access to the Financial Database for some time and is now finalizing arrangements with IRS to provide the bank supervisory agencies and the Securities and Exchange Commission with "on-line" access as well.

Treasury also has extensively revised the guidelines under which the U.S. Customs Service and the Internal Revenue Service may disseminate Bank Secrecy Act data to minimize procedural difficulties for other agencies and to make the data more readily available to Federal, State and foreign agencies.

In addition, Treasury has concluded an agreement with the Office of the Attorney General in California for transmission of magnetic tapes of Currency Transaction Reports that have been filed by California financial institutions. This agreement will allow the State of California to carry out its responsibilities under its own anti-money laundering law, without requiring California financial institutions to file duplicate copies of CTRs with the State.

Digitized by Google

Since last May, Treasury has had an unprecedented level of activity in improvements to the Bank Secrecy Act regulations. First Treasury added the Postal Service to the list of institutions subject to the Bank Secrecy Act We know of your special interest in the subject, because in 98 a former smurf" testified before your Committee on how he purchased Postal Service money orders to launder money Law enforcement authorities in several major cities also observed that money launderers were purchasing Postal Service money orders with substantial amounts of cash. As you know this problem prompted Congress at the urging of this Committee to add the Postal Service to the definition of "financial institution in the Anti-Drug Abuse Act of 986. Accordingly Treasury amended the Bank Secrecy Act regulations on January 13, 1988 to include the Postal Service in the definition of the term financial institutions

We also have taken several other regulatory steps that would be of interest to your Committee:

- o On June 26, 1987, we added a new Subpart to our regulations prescribing procedures for use of our administrative summons authority given to us in the Anti-Drug Abuse Act of 1986.

- o On September 22, 1987, we amended 31 C.F.R. 103 43 to clarify our dissemination authority to governmental authorities of Bank Secrecy Act data and to provide for user fees for disclosures to State and local governmental authorities. The user fees would be used in the situations ike the California agreement that I referred to earlier.

- o On September 22, 1987, we added a new Subpart to our regulations establishing an administrative ruling system which I will discuss later in my testimony.

- o On March 29, 1988, we amended 31 C.F.R. 103.25, the international "targeting" regulation, to permit reporting on retroactive transactions and to prohibit notification by the reporting financial institution of the existence of the reporting requirement to affected parties These amendments will enable us to look at currency flows from the recent past and will ensure that, when we do require reporting on a prospective basi , that the data will not be altered as a result of customers stopping their normal business patterns.

- o We also have pending a Notice of Proposed Rulemaking, issued on April 7, 1988, proposing two amendments to the recordkeeping requirements for casinos. The comment period ended May 9, and we are in the process of drafting a final rule.

Digitized by Google

- We also have several regulatory projects pending. Of special interest to you might be a proposed definition of structuring that will be published as a Notice of Proposed Rulemaking in the next few weeks. In the near future, we also will be issuing a proposed regulation improving the CMIR provisions of the regulations. Finally we soon will be publishing comprehensive revisions of the regulations applicable to casinos to address their unique compliance problems and capabilities.

- Finally, on March 11, 1988, Treasury published an Advanced Notice of Proposed Rulemaking to solicit the views of financial institutions, law enforcement agencies and others on how financial institutions can best provide notice of the anti-structuring provisions of the Bank Secrecy Act to customers of financial institutions. We are in the process of evaluating the comments that we have received on this proposal.

Encouraging Compliance with the Bank Secrecy Act

Treasury has taken a number of steps to facilitate and assure full compliance by all types of financial institutions. Treasury also recognizes that many financial institutions have every interest in complying with the Act s requirements but have legitimate questions about the requirements of the regulations and concerns about the costs associated with compliance. Treasury shares these concerns. To address these concerns, and to make the process of complying with the Act's requirements more efficient, Treasury has undertaken three significant projects.

First, Treasury, with the assistance of the IRS, has written a comprehensive handbook on how to properly exempt certain types of customer accounts and currency transactions from the CTR reporting requirements, as permitted by the regulations. Treasury and the IRS have written this handbook in response to their observation that many banks are over-reporting on exemptible customers, largely because of their concern that they may be penalized if they mistakenly place ineligible customers on their exemption lists. This practice has caused these banks to file many more CTRs that the regulations require The Exemption Handbook which is at tha printers should help to alleviate the banks concerns about the proper use of the exemption provisions of the regulations, and minimize confusion about their proper application. In addition to the booklet Treasury will be corresponding with the 50 largest banks that appear to be under-utilizing the exemption process.

Second, Treasury is about to issue formal administrative rulings on various provisions of the Bank Secrecy Act regulations. These rulings are being issued pursuant to a revision in the Bank Secrecy Act regulations, issued on September 22, 1987, that explains the process for seeking administrative rulings from

Digitized by Google

Treasury. As Treasury responds to various requests for rulings, or issues rulings on its own initiative, it will be able to develop an expanding range of interpretations of the regulations and provide the financial community with clearer guidance on the meaning of the regulations.

Third, on December 31, 1987, Treasury published a notice in the Federal Register that announced the establishment of a permanent program that permits financial institutions to file CTRs on magnetic tape with the IRS Data Center An earlier pilot program confirmed the expected benefits of magnetic tape filing of CTRS, that is an increase in the accuracy of data being reported (only 5% of CTRs filed by magnetic tape contained data inconsistencies or format errors reduction in processing costs (net savings to the government of $22 million over 10 years) and a reduction in the processing time, measured from date of transaction to date first available for agent review (from 45 days to days, an overall reduction of 27 days With the encouragement of Treasury IRS, and the financial community, the program is growing, and we expect Chase Manhattan and Wells Fargo to begin filing by magnetic tape very soon

Financial Enforcement Strategy

I now would like to turn to some of the broader law enforcement interests that influence Treasury's approach to Bank Secrecy Act enforcement Treasury views the Bank Secrecy Act not as a discrete program that can be conducted without reference to the enforcement activities of other Federal agencies but rather as an integral part of a coordinated approach to financial enforcement issues that Treasury the Justice Department, and other Federal law enforcement agencies are now pursuing.

One of the most significant means for developing this coordinated approach is the Financial Enforcement Committee of the National Drug Policy Board, which is chaired by Treasury. The Committee has become increasingly active and visible as the overall coordinating body for government programs that attack the financial operations of drug traffickers.

Two of the Committee's more substantial projects deserve special mention. One is the development and coordination of an interagency Financial Enforcement Training Program that will include Federal, State, and local government training in financial investigation and prosecution techniques. This training program is meant to implement the financial investigations strategy that recognizes the importance of joint financial investigative task forces as a means of attacking the serious drug problem in this country. The strategy recognizes that, in addition to targeting known trafficking organizations, a strategy that follows the money flowing in and out of the trafficking organizations can uncover previously unknown trafficking groups and identify the upper echelons of the organization.

Digitized by Google

The other project is referred to by the Financial Enforcement Committee as the Money Flow Model Project This project is designed to produce a computer simulation model of the money flow mechanisms of drug trafficking and other illegal enterprises. Such a model in the Committee' view, is expected to provide the Policy Board with new analytical tools to aid in the investigation of the money flow that supports illegal activities, to assist in the analysis and development of financial policies to limi illega activities that are supported by illegally obtained funds, to assist in the development of financial enforcement methods, and to improve the quantification of the total volume of llegal financial activity and ts economic effects. The long-range objective of the project is to develop a computer imulation model that can be used by government agencies to plan appropriate action against the assets of major criminals and criminal organizations.

The Money Flow Model Project is being developed for the Financial Enforcement Committee by the Los Alamos National Laboratory. The initial phase of the project, the writing of the plan for the model has been funded by joint contributions from the IRS, Customs, the FBI, and the DEA. The initial phase of the project began in April, 1988, and will run for ninety days

In addition to these two projects, the Financial Enforcement Committee is overseeing a substantial number of other projects, including the cataloging of all financial enforcement training now being conducted, a program for cross-training of intelligence analysts involved in financial analysis, and a task force to explore more effective uses of financial information. All of these initiatives can be expected to yield substantial returns for the Federal Government in investigating, prosecuting, and seeking forfeiture of assets from leading drug traffickers and the money laundering on which they rely.

International Initiatives on Financial Enforcement

While the United States has taken significant steps to deal with the problem of money laundering, the Administration realizes that it must obtain the commitment and cooperation of foreign countries in order to effectively combat drug trafficking and other types of organized criminal enterprises. It is for these reasons that the Administration has raised the narcotics issue with our Summit partners. Narcotics will be discussed in Toronto because of the recognized urgent need for improved international cooperation on programs to counter all aspects of the problem, including its financing, production and trafficking.

The scope and complexity of these issues demand a cooperative international reaction and response. The United States plans to suggest that a special Summit country task force be convened that will include key enforcement, foreign affairs and financial

Digitized by Google

experts who are involved in the battle against narcotics. We will seek improved cooperation across a wide scale of activities and we will also suggest greater efforts in the United Nations and through bilateral treaties with both our Summit partners and other countries. This will be an ongoing process, elements of which are already in place.

In addition, Treasury has recently sent a series of letters to the chief executive officers of U.S.-based financial institutions with foreign branches. These letters set forth the risks associated with international money laundering, identify certain patterns of activity that should be considered suspicious, and encourage the foreign branches of these institutions to report any suspicious transactions to overseas representatives of the IRS and Customs in a manner that is consistent with foreign law. This initiative, which Treasury had promised to pursue in the foreign branches study, may well provide U.S. law enforcement authorities with additional leads in money laundering and Bank Secrecy Act cases, and should help to persuade leading U.S. financial institutions that expanded cooperation with Federal law enforcement authorities is in their interest and the interest of their legitimate customers.

Conclusion

In conclusion, we are fighting a war with many fronts in the battle against money laundering and the criminal enterprises it sustains, but our goals are clear. Treasury shares the goal of this Committee to close the doors of legitimate financial institutions to drug money launderers. We want financial institutions to be partners with Treasury in achieving this goal. In turn, we will act responsibly in balancing law enforcement needs with costs to financial institutions in exercising our regulatory authority. We also seek to maximize efficient and effective use of Bank Secrecy Act data through vigorous enforcement.

Finally, we want to facilitate good compliance by financial institutions through open communication with Treasury, education and guidance. Again, I want to commend this Committee for your continued interest in this most important mission.

I will be pleased to answer any questions that any member of the Committee may have.

Digitized by Google

**Statement of Congressman Doug Barnard
before the Banking Committee
in support of two proposed amendments to
Right to Financial Privacy Act**

I appreciate the Deputy Assistant Attorney General's remarks about the need to amend the Right to Financial Privacy Act. In particular, I want to lend my strong support to (1) the amendment to include "major borrowers" in the records exemption which will be under consideration and (2) the amendment to delete the narrow requirement, which applies to no other documentary evidence, that financial customer records under a grand jury subpoena be actually presented a sitting grand jury, a practice not required nor followed as to all other records.

II. Expansion of the Exemption to Major Borrowers

A recent and lengthy investigation of the Commerce, Consumer, and Monetary Affairs Subcommittee, which I chair, provides ample evidence of the need to add "major borrowers" to the group of persons covered by this very narrow exemption to the Right to Financial Privacy Act. We received evidence and allegations that more and more major borrowers defrauding financial institutions are part of organized crime, either the Mafia types of organized crime or members of conspiracies, sometimes together implicated in several financial institution failures in different parts of the country. We see some of the same names involving failures in Utah, California, Washington State, Texas, Florida, Louisiana, and Kansas, just to give you a flavor of the organized crime involved.

Much of the insider criminal misconduct in financial institutions today involves both insiders and borrowers together, often participating in a joint effort or conspiracy. Often the crucial records making possible the criminal activity, including false loan applications, are the borrower's records, not the insider's records. Yet, the insider can destroy, alter or conceal, these borrower records if the insider is notified under the Act. In these situations, the borrower should be viewed as a/implicit or de facto insider. The ratio of major

Digitized by Google

insider to outsider, usually borrower, fraud has increased significantly. The FDIC advises us that in the past that ratio was 4 to 1, insider to outsider (usually borrower) fraud, but now that ratio has changed 3 to 2, insider to outsider. (One major fraud in the Houston area by a borrower may involve $900 million in losses to the institutions involved.) A large number of the frauds fall in the $500,000 to $1 million range. In fact, we examined a number of examples of borrower frauds in the $300,000 to $900,000 range which significantly contributed to the failure of problem institutions with assets in the $30 to $50 million range.

While I would prefer a dollar threshold lower than $500,000, I will support the Justice Department's proposed amendment on "major" borrowers. We should not allow notification to major borrowers to result in possible alteration or concealment of records or flight from the area, which we have also seen. Without this amendment, the Act will remain a serious impediment to timely and effective law enforcement, often against well-organized criminal elements. I strongly support this narrow exemption in the committee print, but I strongly believe that it should be modified slightly to include major borrowers for these reasons.

II. Amendment to modify presentation of documentation to a grand jury

I think that the Justice Department has made clear the need for this. My subcommittee heard of additional problems with this "physical delivery" requirement. In rural areas, Federal grand juries may sit only once every two months. Having to wait that long can delay many investigations which are often delayed too long because of inadequate resources. There is no sound reason whatsoever for this requirement. It apparently was inserted in the law at the last moment by some person who did not understand the grand jury process, which allows delivery of grand jury material to deputized U.S. Attorneys and FBI agents, which review the material anyway.

Digitized by Google

U.S. Department of Justice

Criminal Division

VT:WCH:JRH:ksw
880007861
Typed: 6/17/88

Office of the Deputy Assistant Attorney General

Washington, D.C. 20530

JUN 20 1988

The Honorable Fernand J. St. Germain
Chairman
Committee on Banking,
Finance and Urban Affairs
House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

During the course of my June 8, 1988 testimony concerning the Right To Financial Privacy Act (RFPA) before the Committee on Banking, Finance and Urban Affairs, you inquired concerning the Empire Savings and Loan Association (Empire) investigation. You requested information concerning the origin of the federal investigation and the effects of the RFPA on that investigation.

Federal law enforcement involvement in the Empire investigation was initiated by a citizen complaint. Soon thereafter, referrals were received on various aspects of the case from the Federal Home Loan Bank Board and the Texas Department of Public Safety.

In view of the restrictions imposed by the RFPA, it was decided to rely almost exclusively on grand jury subpoenas to obtain records needed for the Empire investigation. There were periods of delay and inconvenience due to the production of massive amounts of documents before the grand jury. There was further delay because many institutions, relying on the RFPA, refused to inform us whether or not an account relationship existed without a grand jury subpoena.

Sincerely,

/s/ Victoria Toensing

Victoria Toensing
Deputy Assistant Attorney General
Criminal Division

Records	OEO
Section Chron	OLA
Branch Chron (2)	Pauley
Toensing	
Hochberg	HOLD

Digitized by Google

FERNAND J. ST GERMAIN, RHODE ISLAND, CHAIRMAN
HENRY B. GONZALEZ, TEXAS
FRANK ANNUNZIO, ILLINOIS
WALTER E. FAUNTROY, DISTRICT OF COLUMBIA
STEPHEN L. NEAL, NORTH CAROLINA
CARROLL HUBBARD, JR., KENTUCKY
JOHN J. LAFALCE, NEW YORK
MARY ROSE OAKAR, OHIO
BRUCE F. VENTO, MINNESOTA
DOUG BARNARD, JR., GEORGIA
ROBERT GARCIA, NEW YORK
CHARLES E. SCHUMER, NEW YORK
BARNEY FRANK, MASSACHUSETTS
G. "BOBBY" ROEMER, LOUISIANA
RICHARD H. LEHMAN, CALIFORNIA
BRUCE A. MORRISON, CONNECTICUT
MARCY KAPTUR, OHIO
BEN ERDREICH, ALABAMA
THOMAS R. CARPER, DELAWARE
ESTEBAN E. TORRES, CALIFORNIA
GERALD D. KLECZKA, WISCONSIN
BILL NELSON, FLORIDA
PAUL E. KANJORSKI, PENNSYLVANIA
BART GORDON, TENNESSEE
THOMAS J. MANTON, NEW YORK
ELIZABETH J. PATTERSON, SOUTH CAROLINA
THOMAS McMILLEN, MARYLAND
JOSEPH P. KENNEDY II, MASSACHUSETTS
FLOYD H. FLAKE, NEW YORK
KWEISI MFUME, MARYLAND
DAVID E. PRICE, NORTH CAROLINA
NANCY PELOSI, CALIFORNIA

U.S. HOUSE OF REPRESENTATIVES
COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS
ONE HUNDREDTH CONGRESS
2129 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, DC 20515

CHALMERS P. WYLIE, OHIO
JIM LEACH, IOWA
NORMAN D. SHUMWAY, CALIFORNIA
STAN PARRIS, VIRGINIA
BILL McCOLLUM, FLORIDA
GEORGE C. WORTLEY, NEW YORK
MARGE ROUKEMA, NEW JERSEY
DOUG BEREUTER, NEBRASKA
DAVID DREIER, CALIFORNIA
JOHN HILER, INDIANA
THOMAS J. RIDGE, PENNSYLVANIA
STEVE BARTLETT, TEXAS
TOBY ROTH, WISCONSIN
AL McCANDLESS, CALIFORNIA
J. ALEX McMILLAN, NORTH CAROLINA
JAMES SAXTON, NEW JERSEY
PAT SWINDALL, GEORGIA
PATRICIA SAIKI, HAWAII
JAMES BUNNING, KENTUCKY
JOSEPH J. DioGUARDI, NEW YORK

(202) 226-4247

May 26, 1988

Honorable Edwin Meese III
U.S. Attorney General
Department of Justice
10th and Constitution Avenue N.W.
Washington, D.C. 20530

Dear Mr. Attorney General:

The Committee on Banking, Finance and Urban Affairs invites you, or your designee, to appear and testify at a hearing on Wednesday, June 8, 1988 at 2:00 p.m. in room 2129 of the Rayburn House Office Building.

The subject and purpose of this hearing is to review possible legislative initiatives that fall within the Banking Committee's jurisdiction which are designed to further protect this nation's financial institutions from being used by drug traffickers and money launderers to conceal their illegal profits; and to further aid law enforcement officials in the prevention, detection, and prosecution of those individuals who would use these institutions for their illicit purposes.

As you are aware, Subtitle H, the Money Laundering Control Act of 1986 of the Anti-Drug Abuse Act of 1986 (P.L. 99-570) already attests to the valuable contribution this Committee has made to the anti-drug effort. Unfortunately, more needs to be done.

The Committee is considering among other things, amendments to the Right to Financial Privacy Act which would exempt insiders of financial institutions from the notification requirements stipulated in that Act, permit a financial institution or supervisory agency to provide financial records of any officer, director, employee, or controlling shareholder to the appropriate law enforcement officials, and permit a financial institution or supervisory agency to provide financial records to the Secretary of the Treasury in case of a possible violation of the Bank Secrecy Act.

Digitized by Google

[redacted]

In addition, the Committee is considering the merits of amending the Bank Secrecy Act so as to [redacted] by providing that a financial institution shall require proper identification of persons seeking to purchase a financial instrument over $3,000, and [redacted] by requiring institutions to maintain purchasers' records for inspection and transmission under 31 U.S.C. 5313.

The Committee would appreciate your views on these proposals and any other proposals that you believe have merit and that fall within the Banking Committee's jurisdiction.

The drug problem in America has truly become a national proportions, and the Banking Committee is committed to aiding law enforcement officials in their ever [redacted] fight against this national epidemic.

In accordance with Committee rules, please deliver [redacted] copies of your prepared statement or text of your remarks to Room 2129 Dirksen Senate Office Building, Washington, D.C. 20510, 24 hours in advance of your scheduled appearance. The witnesses in their entirety will be included in the hearing record, and delivered copy requested will be made available to the Committee members in advance of the hearing. It is effort to provide all members with sufficient time for questioning, please limit your oral presentation to that of your testimony to 5 minutes.

Sincerely,

[redacted]

Chairman

[redacted]

Digitized by Google

FERNAND J. ST GERMAIN, RHODE ISLAND, CHAIRMAN
HENRY B. GONZALEZ, TEXAS
FRANK ANNUNZIO, ILLINOIS
WALTER E. FAUNTROY, DISTRICT OF COLUMBIA
STEPHEN L. NEAL, NORTH CAROLINA
CARROLL HUBBARD, JR., KENTUCKY
JOHN J. LAFALCE, NEW YORK
MARY ROSE OAKAR, OHIO
BRUCE F. VENTO, MINNESOTA
DOUG BARNARD, JR., GEORGIA
ROBERT GARCIA, NEW YORK
CHARLES E. SCHUMER, NEW YORK
BARNEY FRANK, MASSACHUSETTS
RUDDY ROEMER, LOUISIANA
RICHARD H. LEHMAN, CALIFORNIA
BRUCE A. MORRISON, CONNECTICUT
NANCY KAPTUR, OHIO
BEN ERDREICH, ALABAMA
THOMAS R. CARPER, DELAWARE
ESTEBAN E. TORRES, CALIFORNIA
GERALD D. KLECZKA, WISCONSIN
BILL NELSON, FLORIDA
PAUL E. KANJORSKI, PENNSYLVANIA
MARY GORDON, TENNESSEE
THOMAS J. MANTON, NEW YORK
ELIZABETH J. PATTERSON, SOUTH CAROLINA
THOMAS MARTIN, MARYLAND
JOSEPH P. KENNEDY II, MASSACHUSETTS
FLOYD H. FLAKE, NEW YORK
KWEISI MFUME, MARYLAND
DAVID E. PRICE, NORTH CAROLINA
NANCY PELOSI, CALIFORNIA

U.S. HOUSE OF REPRESENTATIVES
COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS
ONE HUNDREDTH CONGRESS
2129 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, DC 20515

CHALMERS P. WYLIE, OHIO
JIM LEACH, IOWA
NORMAN D. SHUMWAY, CALIFORNIA
STAN PARRIS, VIRGINIA
BILL McCOLLUM, FLORIDA
GEORGE C. WORTLEY, NEW YORK
MARGE ROUKEMA, NEW JERSEY
DOUG BEREUTER, NEBRASKA
DAVID DREIER, CALIFORNIA
JOHN HILER, INDIANA
THOMAS J. RIDGE, PENNSYLVANIA
STEVE BARTLETT, TEXAS
TOBY ROTH, WISCONSIN
AL McCANDLESS, CALIFORNIA
J. ALEX McMILLAN, NORTH CAROLINA
JAMES SAXTON, NEW JERSEY
PAT SWINDALL, GEORGIA
PATRICIA SAIKI, HAWAII
JAMES BUNNING, KENTUCKY
JOSEPH J. DioGUARDI, NEW YORK

(202) 225-4247

May 26, 1988

Honorable James A. Baker
Secretary of the Treasury
15th Street and Pennsylvania Avenue, N.W.
Washington, D.C. 20220

Dear Mr. Secretary:

The Committee on Banking, Finance and Urban Affairs invites you, or your designee, to appear and testify at a hearing on Wednesday, June 8, 1988 at 2:00 p.m. in room 2129 of the Rayburn House Office Building.

The subject and purpose of this hearing is to review possible legislative initiatives that fall within the Banking Committee's jurisdiction which are designed to further protect this nation's financial institutions from being used by drug traffickers, and money launderers to conceal their illegal profits; and to further aid law enforcement officials in the prevention, detection, and prosecution of those individuals who would use these institutions for their illicit purposes.

As you are aware, Subtitle H, the Money Laundering Control Act of 1986 of the Anti-Drug Abuse Act of 1986 (P.L. 99-570) already attests to the valuable contribution this Committee has made to the anti-drug effort. Unfortunately, more needs to be done.

The Committee is considering among other things, amendments to the Right to Financial Privacy Act which would exempt insiders of financial institutions from the notification requirements stipulated in that Act, permit a financial institution or supervisory agency to provide financial records of any officer, director, employee, or controlling shareholder to the appropriate law enforcement officials, and permit a financial institution or supervisory agency to provide financial records to the Secretary of the Treasury in case of a possible violation of the Bank Secrecy Act.

Digitized by Google

In addition, the Committee is considering the merits of amending the Bank Secrecy Act in at least two instances: (1) by providing that a financial institution shall require proper identification of persons wishing to purchase a financial instrument over $3,000, and (2) by targeting institutions in certain geographic locations for reporting cash transactions under $10,000.

The Committee would appreciate your views on these proposals and any other proposals that you believe have merit and that fall within the Banking Committee's jurisdiction.

The drug problem in America has truly grown to onerous proportions, and the Banking Committee is committed to aiding law enforcement officials in their ever so important fight against this national epidemic.

In accordance with Committee rules, please deliver 200 copies of your prepared statement or that of your designee to Room 2129 Rayburn House Office Building, Washington, D.C. 20515, 24 hours in advance of your scheduled appearance. The statements in their entirety will be included in the hearing record and, if delivered when requested, will be made available to all Committee members in advance of the hearing. In an effort to provide all members with sufficient time for questioning, please limit your oral presentation or that of your designee to 5 minutes.

Sincerely,

Fernand J. St Germain
Chairman

FJStG:dk

Digitized by Google

DEPOSIT
AUG 09 1988
SHIPPED

Digitized by Google

Y 4.B 22/1:100-70 C.1
Money Laundering Contr
Stanford University Libraries
3 6105 045 154 858

DATE DUE

STANFORD UNIVERSITY LIBRARIES
STANFORD, CALIFORNIA 94305-6004

Digitized by Google

Digitized by Google